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No. 99-___

In The

Supreme Court of the United States

AT&T CORP. AND
MCI WORLDCOM NETWORK SERVICES, INC.,
Petitioners,

v.

CINCINNATI BELL TELEPHONE COMPANY,
Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

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APPENDIX A

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v.

FEDERAL COMMUNICATIONS COMMISSION and United States of America, Respondents.

No. 97-60421.

United States Court of Appeals,
Fifth Circuit.

July 30, 1999.

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Petitions for Review of a Final Order of the Federal Communications Commission.

Before SMITH, DUHÉ and EMILIO M. GARZA, Circuit Judges.

JERRY E. SMITH, Circuit Judge:

This is a consolidated challenge to the most recent attempt of the Federal Communications Commission ("FCC") to implement provisions of the landmark 1996 Telecommunications Act (the "Act").[1] Petitioners, joined by numerous intervenors, challenge several aspects of the FCC's Universal Service Order (the "Order") implementing the provisions of the Act codified at 47 U.S.C. § 254. We grant the petition for review in part, deny it in part, affirm in part, reverse in part, and remand in part.

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[1] Telecommunications Act of 1996, Pub.L. No. 104-104, 110 Stat. 56 (to be codified as amended in scattered sections of title 47, United States Code).

I. Background.

A. The 1996 Act and the Universal Service Order.

Beginning with the passage of the Communications Act of 1934 (the "1934 Act"), Congress has made universal service a basic goal of telecommunications regulation. As Section 1 of the 1934 Act stated, the FCC was created

> [f]or the purpose of regulating interstate and foreign commerce in communication by wire and radio so as to make available, so far as possible, to all the people of the United States, without discrimination on the basis of race, color, religion, national origin, or sex, a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges. . . .

47 U.S.C. § 151 (as amended).

Armed with this statutory mandate, the FCC historically has focused on increasing the availability of reasonably priced, basic telephone service via the landline telecommunications network.[2] Rather than relying on market forces alone, the agency has used a combination of implicit and explicit subsidies to achieve its goal of

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[2] In economic terms, universal service programs are justified as a way to address a "market failure." While the carriers have little incentive to expand the telecommunications infrastructure into areas of low population density or geographic isolation, each individual user of the network benefits from the greatest possible number of users. *See* Eli M. Noam, *Will Universal Service and Common Carriage Survive the Telecommunications Act of 1996?*, 97 Colum. L.Rev. 955, 958-59 (1997).

greater telephone subscribership. Explicit subsidies provide carriers or individuals with specific grants that can be used to pay for or reduce the charges for telephone service. This form of subsidy includes using revenues from line charges on end-users to subsidize high-cost service directly and to support the Lifeline Assistance program for low-income subscribers.

Implicit subsidies are more complicated and involve the manipulation of rates for some customers to subsidize more affordable rates for others. For example, the regulators may require the carrier to charge "above-cost" rates to low-cost, profitable urban customers to offer the "below-cost" rates to expensive, unprofitable rural customers.

For obvious reasons, this system of implicit subsidies can work well only under regulated conditions. In a competitive environment, a carrier that tries to subsidize below-cost rates to rural customers with above-cost rates to urban customers is vulnerable to a competitor that offers at-cost rates to urban customers. Because opening local telephone markets to competition is a principal objective of the Act, Congress recognized that the universal service system of implicit subsidies would have to be re-examined.

To attain the goal of local competition while preserving universal service, Congress directed the FCC to replace the patchwork of explicit and implicit subsidies with "specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service." 47 U.S.C. § 254(b)(5). Congress also specified new universal service support for schools, libraries, and rural

health care providers. *See* 47 U.S.C. § 254(h). It then directed the FCC to define such a system and to establish a timetable for implementation within fifteen months of the passage of the Act.

The Federal-State Joint Board (the "Joint Board"), created by the Act to coordinate federal and state regulatory interests, issued two recommendations on how to implement the universal service provisions.[3] The FCC met the statutory deadline when it issued the Order on May 8, 1997.[4] Since that time, the agency has issued seven reconsideration orders (the last one on May 28, 1999) and has made two reports to Congress regarding the Order.

The FCC designated a set of core services eligible for universal service support, proposed a mechanism for supporting those services, and established a timetable for

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[3] The first Recommended Decision was issued on November 8, 1996 (12 FCC Rcd 87 (1996)), the second Recommended Decision on November 25, 1998 (13 FCC Rcd 24744 (1998)).

[4] Congress also directed that the FCC establish rules to achieve the local competition goals of the Act within six months of the Act's enactment. The agency met this deadline when it issued the Local Competition Order on August 8, 1996. Almost all parts of this order were affirmed by the Supreme Court. *See AT & T v. Iowa Utils. Bd.*, 525 U.S. 366, 119 S.Ct. 721, 142 L.Ed.2d 835 (1999).

On the same day it issued the Order, the FCC released the Access Charge Order. Access charges are the charges assessed between local exchange companies (LEC's) and interexchange companies (IXC's) for the use of one network by callers from the other network. Challenges to this order were also consolidated before the Eighth Circuit. *See Southwestern Bell Tel. Co. v. FCC*, 153 F.3d 523 (8th Cir.1998).

implementation. See Order ¶¶ 21-42. Pursuant to the Act, the agency developed rules for modifying the existing system of support for high-cost service areas and created new support programs for schools, libraries, and health care facilities.

1. HIGH-COST SUPPORT.

The FCC's plans for changing the high-cost support system required it to resolve a number of complicated issues, including (1) what methodology to use for calculating high-cost support; (2) how to allocate costs between the states and the federal government; (3) which carriers should be required to contribute to the support system; and (4) when to implement the high-cost support program. The agency resolved the question of how to calculate the proper amount of high-cost support by accepting the Joint Board's second recommendation to identify areas where the forward-looking cost of service exceeds a cost-based benchmark and to provide extra support to any state that cannot maintain reasonable comparability.[5] See Second Recommended Decision ¶ 19; Seventh Report and Order ¶ 61 n.157.

Most importantly, the FCC decided to use the "forward-looking" costs to calculate the relevant costs of a carrier

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[5] This methodology is a departure from the revenue-based national benchmark proposed in the Order. The revenue-based benchmark was challenged for including discretionary revenues in its calculation and for its nationwide scope. Because of the revisions proposed by the Joint Board's Second Recommended Decision, we now consider those challenges to the prior revenue-based methodology moot. *See infra* part III.A.1.b.

serving a given geographical area. In other words, to encourage carriers to act efficiently, the agency would base its calculation on the costs an efficient carrier would incur (rather than the costs the incumbent carriers historically have incurred).[6]

The FCC developed rules for determining which carriers should be required to contribute to the interstate universal service support system and how their contributions should be calculated. It decided to require all telecommunications carriers and certain non-telecommunications carriers to contribute in proportion to their share of end-user telecommunications revenues. *See* Order

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[6] The agency made a decision to provide only 25% of the funds for high-cost support, leaving the state commissions ("the states") to provide the rest of the funds. According to the FCC, the states traditionally have provided a majority of universal service support, and if the agency were to fund all the high-cost support, it would overcompensate carriers. Moreover, the FCC claims that the 25% figure approximates the costs that historically have been assigned to the interstate jurisdiction. *See* Order ¶ 201.

The Joint Board, however, recommended that the FCC scrap the 25%/75% division of responsibility in favor of a more flexible plan of allocation. *See* Second Recommended Decision ¶¶ 4-5, 41-46. The FCC accepted the Joint Board's recommendation and eliminated the 25/75 rule on May 27, 1999, thereby mooting the issue for this court. *See infra* part III.A.1.c. *See also Seventh Report and Order* ¶ 3 ("We explicitly reconsider and repudiate any suggestion in the *First Report and Order* that federal support should be limited to 25 percent of the difference between the benchmark and forward-looking cost estimates. . . . ").

¶¶ 39-42. The agency determined that to reduce the burden on individual carriers' prices, the carriers' contribution base should be as broad as possible. *See* Order ¶ 783. Therefore, the agency required contributing carriers to include their international telecommunications revenues in their contribution base and rejected claims by certain carriers,[7] which do not receive direct subsidies from the support program, seeking an exemption from making any contributions. *See* Order ¶ 805.

Finally, the FCC adopted a timetable for implementing its high-cost support plan. Because it has not yet developed an accurate assessment of forward-looking costs, it delayed implementation of its support program for non-rural carriers until January 1, 2000.[8] Additionally, because the agency believes it will take even longer to develop accurate forward-looking cost models for rural carriers, it delayed the implementation of its new support plan for rural carriers to "no sooner than January 1, 2001." *See* Order ¶ 204.

During this delay in implementation, the FCC decided that carriers will continue to receive support at the levels generated by existing universal support programs. According to the agency, this gradual, phased-in

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[7] These carriers include wireless service providers of paging and commercial mobile radio service ("CMRS"). The FCC also rejected a claim by CMRS providers seeking an exemption from making contributions to state support funds.

[8] In the original order, the FCC had planned implementation by January 1, 1999. This date was delayed until July 1, 1999, and again to January 1, 2000. *See Seventh Report and Order* ¶ 5.

plan for implementing its new high-cost support system meets the Act's requirement of a "specific timetable for completion." *See* 47 U.S.C. § 254(a)(2).

2. Schools and Libraries.

Pursuant to § 254(h), the FCC adopted rules implementing new programs for schools, libraries, and health care facilities, in particular by providing universal service support for internet access and internal connections in schools and libraries. *See* Order ¶ 436. The agency decided that any entity, including non-telecommunications carriers, that provides internet access or internal connections to schools and libraries will receive universal service support. *See* Order ¶ 594.

To fund the new § 254(h) programs, the FCC accepted the Joint Board's recommendation to assess the interstate *and* intrastate revenues of providers of interstate telecommunications service. *See* Order ¶ 808. Because many states do not already have similar support programs for schools and libraries, the agency justified its inclusion of intrastate revenues as necessary to ensure adequate funding for § 254(h) programs.

B. Challenges to the Order.

On September 5, 1997, petitioner Celpage Inc. filed a motion in this court to stay the Order. We denied that motion on October 16, 1997, and rejected a similar motion by various rural telephone companies on December 31, 1997. Their petitions, along with challenges to the Order by other petitioners, were consolidated in this court.

There are two sets of challenges to the Order. The first regards the FCC's plan for replacing the current mixture of explicit and implicit subsidies with an explicit universal service support system for high-cost areas. On both statutory and constitutional grounds, petitioners attack (1) the methodology for calculating support under the plan; (2) the allocation of funding responsibilities between the FCC and the states; and (3) the agency's restrictions on how carriers can recover universal service costs.

Other petitioners attack the FCC's high-cost support plan as an encroachment on state authority over intrastate telecommunications regulation because it restricts state eligibility requirements and imposes a "no disconnect" rule for low-income telephone subscribers. Petitioners also challenge, for lack of specificity and for failing to delay implementation of the plan for some rural carriers, the FCC's timetable for implementing the new universal service plan. Additionally, petitioners challenge the FCC's system for assessing contributions, arguing that it improperly includes CMRS providers and unfairly assesses carriers on the basis of their international and interstate revenues.

The second set of challenges regards the FCC's proposal for implementing § 254(h) programs supporting schools, libraries, and health care providers. Petitioners claim that the FCC impermissibly expanded the scope of § 254(h) support to include the provision of internet access and internal connections. Moreover, they attack the FCC's statutory authority to provide such support to non-telecommunications providers.

Additionally, petitioners charge that the agency encroached on state authority to implement state support programs for schools and libraries and failed to designate which telecommunications services will receive § 254(h) support. They also argue that the FCC exceeded its statutory authority by requiring subsidies for toll-free telephone calls to internet service providers by non-rural health care providers. Finally, they attack the FCC's § 254(h) contribution system because it assesses both the intrastate and interstate revenues of carriers.[9]

We affirm most of the FCC's decisions regarding its implementation of the high-cost support system, concluding, for the most part, that the Order violates neither the statutory requirements nor the Constitution. We remand for further consideration, however, as to the FCC's decision to assess contributions from carriers based on both international and interstate revenues. We also reverse (1) the requirement that ILEC's recover their contributions from access charges and (2) the blanket prohibition on additional state eligibility requirements for carriers receiving high-cost support.

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[9] The FCC also determined that it could require carriers to contribute, based on both interstate and intrastate revenues, to high-cost support as well as § 254(h) support. But for policy reasons, it decided to assess contributions on both interstate and intrastate revenues for support of § 254(h) programs only. It maintains, however, that it may impose similar assessments for high-cost support as well. *See Seventh Report and Order* ¶¶ 87-90.

We review the states' challenge to the FCC's claim of jurisdictional authority over intrastate rates in the context of its actions regarding support of the § 254(h) programs, but we also discuss its implications for FCC jurisdictional authority for support of high-cost programs. *See infra*, part III.B.6.

On jurisdictional grounds, we reverse the rule prohibiting local telephone service providers from disconnecting low-income subscribers. We also conclude that the agency exceeded its jurisdictional authority when it assessed contributions for § 254(h) "schools and libraries" programs based on the combined intrastate and interstate revenues of interstate telecommunications providers and when it asserted its jurisdictional authority to do the same on behalf of high-cost support.

II. Standard of Review.

When deciding whether the FCC has the statutory authority to adopt the rules included in the Order, we review the agency's interpretation under *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 104 S.Ct. 2778, 81 L.Ed.2d 694 (1984), by first deciding whether "Congress has directly spoken to the precise question at issue," *id.* at 842, 104 S.Ct. 2778. If so, we "give effect to the unambiguously expressed intent of Congress." *Id.* at 842-43, 104 S.Ct. 2778. In this situation, we reverse an agency's interpretation if it does not conform to the plain meaning of the statute. This level of review is often called "*Chevron* step-one" review.

Where the statute is silent or ambiguous, however, "the question for the court is whether the agency's answer is based on a permissible construction of the statute." *Id.* at 843, 104 S.Ct. 2778. We may reverse the agency's construction of an ambiguous or silent provision only if we find it "arbitrary, capricious or manifestly contrary to the statute." *Id.* at 844, 104 S.Ct. 2778. That is to say, we will sustain an agency interpretation of an

ambiguous statute if the interpretation "is based on a permissible construction of the statute." *Id.* at 843, 104 S.Ct. 2778. We refer to this more deferential level of review as "*Chevron* step-two" review.

The Administrative Procedure Act ("APA") also authorizes us to reverse an agency's action if it acted arbitrarily or capriciously in adopting its interpretation by failing to give a reasonable explanation for how it reached its decision. *See* 5 U.S.C. § 706(2)(A) (1994); *see also Harris v. United States*, 19 F.3d 1090 (5th Cir.1994). "Arbitrary and capricious" review under the APA differs from *Chevron* step-two review, because it focuses on the reasonability of the agency's decision-making processes rather than on the reasonability of its interpretation.[10]

Finally, we do not give the FCC's actions the usual deference when reviewing a potential violation of a constitutional right. "The intent of Congress in 5 U.S.C. § 706(2)(B) was that courts should make an independent assessment of a citizen's claim of constitutional right when reviewing agency decision-making." *Porter v. Califano*, 592 F.2d 770, 780 (5th Cir.1979).

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[10] *See Arent v. Shalala*, 70 F.3d 610, 614-16 (D.C.Cir.1995); *see also* Gary Lawson, *Outcome, Procedure and Process: Agency Duties of Explanation for Legal Conclusions*, 48 RUTGERS L.REV. 313 (1996). We recognize the difference between *Chevron* step-two review and the APA's arbitrary and capricious review is not always obvious. Indeed, the different standards of review overlap, because both require a reviewing court to decide whether the agency action is "manifestly contrary to the statute" (*Chevron*) or "otherwise not in accordance with law." (APA). *See Arent*, 70 F.3d at 615 & n. 6.

III. Analysis.

A. High-Cost Support.

1. Methodology for Calculating Support for High-cost Areas.

a. Forward-looking Cost-of-Service Methodology.

GTE and Southwestern Bell (collectively "GTE") and the FCC engage in a fairly complex economic debate over the merits of calculating costs using the forward-looking cost models based on the "least cost, most efficient" carrier.[11] Because incumbent local exchange carriers

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[11] As an initial matter, the FCC asks us to dismiss all challenges to its methodology for calculating high-cost support, claiming that such challenges are not ripe in light of the Joint Board's Second Recommended Decision. The Joint Board advised the agency to make substantial revisions in the high-cost support methodology, including the elimination of the 25%/75% division between federal and state contributions and the modification of the revenue benchmark used to calculate high-cost support. The FCC accepted these recommendations, and we dismiss challenges to those issues as moot. *See infra* parts III.A.1.b and c.

But the FCC did not modify other portions of the Order, including its use of forward-looking cost models. *See Seventh Report and Order* ¶ 48. We agree with GTE that the mere existence of a Joint Board recommendation does not permit the FCC to block all judicial review of its high-cost methodology, especially after the agency has issued its order implementing these recommendations.

The Supreme Court has consistently endorsed judicial review of final agency actions. "Although . . . the FCC regulation could properly be characterized as a statement only of intentions, the Court held that 'such regulations have the

("ILEC's") such as GTE will receive their subsidies, under the new system, based on the difference between the costs of providing service to a high-cost region and the revenue that could be derived from that service, GTE fears that using the costs of a hypothetical most-efficient carrier will significantly reduce the amount of universal service support it receives.

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force of law before their sanctions are invoked as well as after. When, as here, they are promulgated by order of the Commission and the expected conformity to them causes injury cognizable by a court of equity, they are appropriately the subject of attack. . . . ' " *Abbott Lab. v. Gardner*, 387 U.S. 136, 150, 87 S.Ct. 1507, 18 L.Ed.2d 681 (1967) (quoting *Columbia Broadcasting Sys. v. United States*, 316 U.S. 407, 418-19, 62 S.Ct. 1194, 86 L.Ed. 1563 (1942)).

Additionally, we consider four factors when evaluating a claim of lack of ripeness in the administrative context: (1) whether the issues are purely legal; (2) whether the issues are based on a final agency action; (3) whether the controversy has a direct and immediate impact on the plaintiff; and (4) whether the litigation will expedite, rather than delay or impede, effective enforcement by the agency. *See Dresser Indus. v. United States*, 596 F.2d 1231, 1235 (5th Cir.1979). To find a case ripe, we require the party bringing the challenge (here, GTE) to establish all four factors in seeking judicial review. *See Merchants Fast Motor Lines, Inc. v. Interstate Commerce Comm'n*, 5 F.3d 911, 920 (5th Cir.1993).

The FCC does not claim that the issues presented are not purely legal, and we have already explained why, under *Abbott Laboratories*, the Order remains a final agency action. There is no indication that the petitioners are currently unaffected by the legal force of the Order. Finally, we agree with GTE that because the FCC has had ample time (three years) and opportunity to implement the Order, judicial guidance on the legality of the Order will not delay or impede the agency's ability to carry out its statutory duties.

i. STATUTORY INTERPRETATION.

The question, of course, is not whether it is good policy for the FCC to use such cost models,[12] but whether the decision to adopt this methodology conforms to the plain language of the statute. If the language is ambiguous, we must then ask whether the use of forward-looking cost models is reasonable given the terms of the

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[12] GTE refers us to Justice Brandeis's dissent (joined by Justice Holmes) in *Missouri ex rel. Southwestern Bell Tel. Co. v. Public Serv. Comm'n*, 262 U.S. 276, 43 S.Ct. 544, 67 L.Ed. 981 (1923), criticizing use of "fair value" (another version of forward-looking cost models) in ratemaking. GTE notes that Justice Breyer has endorsed Justice Brandeis's criticisms. Even in his separate opinion in *Iowa Utilities*, however, Justice Breyer did not advocate that the Court prohibit the FCC from adopting forward-looking cost models. *See Iowa Utilities*, 119 S.Ct. at 752 (Breyer, J., concurring in part and dissenting in part) ("These examples do not show that the FCC's rules are themselves unreasonable").

Most importantly, the Brandeis criticism of "fair value" has never reflected the view of a majority of the Court, which on several occasions has declined to adopt Justice Brandeis's views on this question. *See Federal Power Comm'n v. Texaco Inc.*, 417 U.S. 380, 94 S.Ct. 2315, 41 L.Ed.2d 141 (1974); *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 64 S.Ct. 281, 88 L.Ed. 333 (1944). Instead, the Court consistently has refused to "designat[e][ ] a single theory of ratemaking [that] would unnecessarily foreclose alternatives which could benefit both consumers and investors." *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 316, 109 S.Ct. 609, 102 L.Ed.2d 646 (1989).

In fact, the Court has explicitly sustained similar cost models not based on historical costs. *See Mobil Oil Exploration & Producing Southeast Inc. v. United Distrib. Cos.*, 498 U.S. 211, 224-25 n. 5, 111 S.Ct. 615, 112 L.Ed.2d 636 (1991) (indicating that similar non-historical based cost model was not arbitrary, capricious, or manifestly contrary to the statute at issue.).

statute and the deference the FCC must be afforded under *Chevron*. Additionally, we must consider whether the agency's actions in reaching its decision are "arbitrary and capricious" under the APA. *See* 5 U.S.C. § 706(2)(A).

We conclude that the plain language is ambiguous as to whether the FCC's cost models are permitted. We then decide that under *Chevron* step-two, the FCC's forward-looking cost models are authorized under their reasonable interpretations of the statutory language. Finally, we do not conclude that the FCC acted in a "arbitrary and capricious" manner in reaching its decision to adopt forward-looking cost models.

GTE argues that the methodology violates the "equitable and nondiscriminatory" language in § 254(b)(4). We disagree with GTE's claim that the plain language of § 254(b)(4) prohibits the FCC from adopting its methodology.

The section of the statute that GTE relies on represents one of seven principles identified by the statute as the basis for the agency's universal service policies. Rather than setting up specific conditions or requirements, § 254(b) reflects a Congressional intent to delegate these difficult policy choices to agency discretion: "The Joint Board and the Commission *shall base policies* for the preservation and advancement of universal service on the following principles. . . . " (Emphasis added.) 47 U.S.C. § 254(b).

Moreover, the FCC has offered reasonable explanations for how its use of the forward-looking cost models cannot be characterized as inequitable and discriminatory. For instance, the FCC points out that all carriers,

including interexchange carriers ("IXC's") such as AT & T and MCI, are subject to the same cost methodology and must move toward the same efficient cost level to maximize the benefits of universal service support.

The term "sufficient" appears in § 254(e), and the plain language of § 254(e) makes sufficiency of universal service support a direct statutory command rather than a statement of one of several principles. Still, we do not find that the use of the single word "sufficient," even in the language of command, demonstrates Congress's unambiguous intent regarding the forward-looking cost models. We therefore review under *Chevron* step-two and conclude that the agency has offered reasonable justifications for its adoption of the "most efficient" methodology.

The FCC points to cases in which agencies have adopted similar methodologies to encourage competition.[13] It also argues that nothing in the statute defines "sufficient" to mean that universal service support must equal the actual costs incurred by ILEC's. These reasons suffice to survive the reasonableness requirement of *Chevron* step-two.

To be sure, the FCC's reason for adopting this methodology is not just to preserve universal service. Rather, it is also trying to encourage local competition by setting

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[13] *See, e.g., West Tex. Util. Co. v. Burlington N.R.R.*, Docket No. 41191 (Surface Transp. Bd. May 3, 1996), *aff'd sub nom. Burlington N.R.R. v. Surface Transp. Bd.*, 114 F.3d 206, 213 (D.C.Cir.1997) (sustaining, as reasonable, agency application of "stand alone cost constraints" based on rates that a hypothetical carrier would have to charge to earn a reasonable return).

the cost models at the "most efficient" level so that carriers will have the incentive to improve operations. As long as it can reasonably argue that the methodology will provide sufficient support for universal service, however, it is free, under the deference we afford it under *Chevron* step-two, to adopt a methodology that serves its other goal of encouraging local competition.

ii. "Arbitrary and Capricious."

Arguing that the FCC has departed from its own stated methodology, GTE charges the agency with "arbitrary and capricious" actions under the APA. *See* 5 U.S.C. § 706(2)(A). The APA's "arbitrary and capricious" standard of review is narrow and requires only a finding that the agency "articulate[d] a rational relationship between the facts found and the choice made." *Harris v. United States*, 19 F.3d 1090, 1096 (5th Cir.1994).

GTE points out that while the agency has wedded itself to the "most efficient" carrier cost methodology, it used current depreciation schedules to develop its models for projecting forward-looking costs. These schedules are not based on the actual costs of the current regulated system, but, GTE contends, have been artificially deflated by state regulators so that local carriers recover less than they would in a real, competitive market. Using these artificially-deflated schedules in the cost models disadvantages the ILEC's, because they will not be able to recover their capital costs as they would if free from regulation.

Actually, the FCC has departed from its general "most efficient" methodology by making a number of adjustments to its cost model. For instance, instead of assuming the "most efficient" wire center locations in its cost models, the agency simply made calculations based on whatever wire centers already exist. *See* Order ¶ 251(1). This allowance actually benefits the ILEC's.

While GTE argues that the FCC's failure to adhere tightly to its "most efficient" methodology fails the "arbitrary and capricious" test, that test, properly understood, is far less onerous. If the FCC's departures from its methodology "articulate a rational relationship," we will not apply the "arbitrary and capricious" remedy.

The FCC seeks to mitigate the effect of the "most efficient" methodology by accounting for wire centers that already exist. Additionally, and contrary to GTE's assertions, the agency is prescribing a range within which the depreciation schedules must fall, rather than simply adopting the schedules that already exist. For the time being, the FCC will rely on the actual depreciation schedules, because it does not see a prospect of significant competition in the near future in the high-cost markets. *See* Order ¶ 250(5). Moreover, the agency has committed itself to re-prescribe the range for these schedules every three years. *See id.* ¶ 250(5) n. 662. These reasons establish enough of a "rational relationship" with facts presented for the forward-looking cost methodology to pass the APA's arbitrary and capricious test.[14]

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[14] GTE claims that implementing the forward-looking cost methodology will force ILEC's to operate at a loss, and this

b. Methodology for Calculating the Revenue Benchmark.

GTE challenged the inclusion of revenues from "discretionary" services in the revenue benchmark used to compare costs and revenues for the purposes of universal service support. The Joint Board, however, recently proposed eliminating the entire revenue benchmark in favor of a single national cost benchmark. *See* Second Recommended Decision ¶¶ 41-50. The FCC accepted this recommendation. *See Seventh Report and Order* ¶ 61 ("[W]e reconsider and reject the determination in the *First Report and Order* that federal support for rate comparability should be determined using a revenue-based benchmark.").[15] This decision moots GTE's challenge to

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constitutes an unconstitutional taking under *Brooks-Scanlon*. GTE's claim has no merit; it has not shown that a taking has occurred or that any taking will be permanent or would be so serious as to be considered "confiscatory." *See Duquesne*, 488 U.S. at 314, 109 S.Ct. 609. ("[A]n otherwise reasonable rate is not subject to constitutional attack by questioning the theoretical consistency of the method that produced it.").

Unlike the situation in *Brooks-Scanlon*, the circumstance here is that the regulatory entity setting the rules, the FCC, is not requiring the ILEC's to remain open or to charge low rates, thereby forcing them to operate at a permanent loss. *See Continental Air Lines v. Dole*, 784 F.2d 1245, 1251 (5th Cir.1986) (distinguishing *Brooks-Scanlon* where agency required loss-making operation for a limited time only).

[15] Vermont has filed a petition for review of the *Seventh Report and Order* in the District of Columbia Circuit. See No. 99-1243 (D.C.Cir.). Pursuant to 28 U.S.C. § 2349(a), it thereby has vested that court with exclusive jurisdiction to review the *Seventh Report and Order*. Unless the District of Columbia Circuit

the inclusion of discretionary revenues, because no revenues will be used in the calculation of the benchmark.[16]

A case becomes moot if (1) there is no reasonable expectation that the alleged violation will recur and (2) interim relief or events have completely and irrevocably eradicated the effects of the alleged violation. *County of Los Angeles v. Davis*, 440 U.S. 625, 631, 99 S.Ct. 1379, 59 L.Ed.2d 642 (1979).[17] The FCC's new approach eradicates

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transfers the petition to this court pursuant to 28 U.S.C. § 2112(a), we lack jurisdiction to consider the order on its merits.

We still retain jurisdiction to the extent that the new order changes or affects the Order that is the subject of this consolidated proceeding. As we explain below, the FCC's repudiation of its revenue benchmarks and the 25% allocation moot the petitioners' challenges for purposes of this appeal. Petitioners, however, are not precluded, by our dismissal in this proceeding, from filing appeals of the new cost-based benchmark and the new allocation methodology in another proceeding.

[16] Mootness goes to the heart of our jurisdiction under Article III of the Constitution. Therefore, we must consider mootness even if the parties do not raise it, because "resolution of this question is essential if federal courts are to function within their constitutional spheres of authority." *North Carolina v. Rice*, 404 U.S. 244, 245, 92 S.Ct. 402, 30 L.Ed.2d 413 (1971).

[17] Even if these conditions are met, there are at least three exceptions to the mootness doctrine. First, courts may assert jurisdiction if the official action being challenged is capable of "repetition, yet evading review." *See Nader v. Volpe*, 475 F.2d 916, 917 (D.C.Cir.1973). Second, courts also have adjudicated otherwise moot issues if the defendant has voluntarily ceased the challenged activity to avoid judicial resolution and there is a reasonable possibility that the challenged conduct will resume. *See Gluth v. Kangas*, 951 F.2d 1504, 1507-08 (9th Cir.1991) (refusing to hold voluntary cessation of prison library

any possible effect of discretionary revenues on the levels of the petitioners' universal service support.[18] We therefore dismiss, as moot, GTE's challenge to the use of discretionary revenues in the high-cost support benchmark.

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restrictions moot in light of long history of policy). Finally, courts have avoided mootness where the mooted issue still has collateral or future consequences. *See Super Tire Eng'g Co. v. McCorkle*, 416 U.S. 115, 122, 94 S.Ct. 1694, 40 L.Ed.2d 1 (1974) (refusing to moot employer's challenge to state benefits for strikers even though strike had ended, because issue would affect employer's future relations with union).

Only the first and second exceptions are arguably applicable to the FCC's new order, and we do not think either exception applies. The "repetition" exception will not apply unless there is a reasonable expectation that the same litigant will again be subjected to the same action. *See DeFunis v. Odegaard*, 416 U.S. 312, 315-17, 94 S.Ct. 1704, 40 L.Ed.2d 164 (1974) (mooting student's lawsuit because he will graduate regardless of outcome of litigation). The second exception requires a showing that the challenged conduct will resume. There is little basis for suggesting that the FCC, after a long and torturous process involving a recommendation from the Joint Board and months of deliberation, will reverse itself on the question of revenue benchmarks.

[18] Reconsideration of agency actions by the implementing agency can moot issues otherwise subject to judicial review because the reviewing court can no longer grant effective relief. *See, e.g., Center for Science in the Pub. Interest v. Regan*, 727 F.2d 1161, 1164 (D.C.Cir.1984) (holding that a change in position of Department of Treasury regarding labeling of alcoholic beverages mooted federal appeal); *see also* 15 JAMES W. MOORE, MOORE'S FEDERAL PRACTICE § 101.96, at 101-179 (3d ed. 1998) ("[A] parallel proceeding in another forum and [ ] resolution of that controversy in that forum will moot the issues presented in the federal action. . . . regardless of whether or not that parallel forum is an administrative proceeding.").

GTE also challenged the FCC's use of a national benchmark for purposes of revenue calculations. Because GTE's challenge focused on the problems of a national *revenue* benchmark, the FCC's elimination of the revenue benchmark also moots its challenge to the national benchmark.

GTE's basic attack on the national revenue benchmark is that ILEC's operating in states with below-average revenues will be systematically undercompensated by a universal service support system based on a national revenue benchmark. But none of these arguments necessarily applies to a cost-based national benchmark.[19] Indeed, the FCC adopted the cost-based national benchmark because it agreed that "revenues may not accurately reflect the level of need for support to enable reasonably comparable rates because states have varying rate-setting methods and goals." *Seventh Report and Order* ¶ 62.

Because the subject matter of GTE's appeal – a national *revenue* benchmark – no longer has any legal force, "[a]ny further judicial pronouncements . . . would be purely advisory." *See Center for Science in the Public Interest*, 727 F.2d at 1164. "We cannot assume jurisdiction to decide a case on the ground that it is the *same* case as one presented to us, when it is admitted that it is not and when it presents different issues." *Id.* at 1166 n. 6

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[19] *Accord Center for Science in the Pub. Interest*, 727 F.2d at 1164 ("Most of the issues presented in these appeals are not necessarily pertinent to examination of the second [administrative action] and may well prove irrelevant in that context.").

(emphasis added). Therefore, we also dismiss, as moot, the challenges to the FCC's national revenue benchmark.[20]

c. Limiting the Federal Mechanism to Twenty-five Percent of Universal Service Costs.

The third step in the FCC's methodology for calculating support to high-cost, non-rural areas allocates 25% of

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[20] Our conclusion regarding mootness does not conflict with *Natural Resources Defense Council v. EPA*, 489 F.2d 390 (5th Cir.1974), in which we refused to moot a challenge to the EPA's approval of Georgia's Clean Air Act implementation plan despite the EPA's later decision to withdraw its approval. Because the EPA's reasons for withdrawing approval showed that it still fundamentally disagreed with the petitioners' interpretation of the Clean Air Act's requirements, we asserted jurisdiction.

In this case, the FCC's new order not only alters, but explicitly repudiates, the reasoning behind its use of *revenues* in calculating the benchmark. All of the petitioners' challenges to the benchmark calculations focused on the unreliability or unfairness of such revenue-based calculations. By eliminating the use of *revenues*, the petitioners and the FCC no longer fundamentally disagree on the problems that revenues cause in calculating the benchmark for high-cost support.

Thus, *Natural Resources Defense Council* does not conflict with the reasoning of *Center for Science in the Public Interest*, 727 F.2d at 1166, in which the court mooted a challenge after the Treasury had implemented a new, superseding regulation containing different reasoning and substantive provisions different from the challenged regulation. In both cases, the courts analyzed whether the intervening agency action represented a substantive shift in an agency's interpretation of its statutory duties.

the funding responsibility to the agency, leaving 75% to be provided by the states. In other words, only 25% of the overall funds for the explicit universal support program for high-cost areas will be provided from the funds collected from interstate telephone calls; the rest must be provided by the states, usually through charges on intrastate service. Certain states,[21] GTE, and Kansas and Vermont[22] challenged this allocation on statutory grounds. Specifically, they question the 25% rule for failing to provide "sufficient" support under § 254(e). Kansas and Vermont also challenged the FCC's 25% allocation decision for lack of notice and for failing to ensure reasonable comparability between rural and urban rates.

As in the case of arguments against the revenue benchmark, we do not consider these challenges, because the FCC has accepted the Joint Board's recommendation to scrap the 25%/75% rule.[23] The *Seventh Report and Order* proposes a new methodology that places "no artificial limits on the amount of federal support that is available"

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[21] Nine state commissions – from Texas, California, Florida, Iowa, Louisiana, New York, Nevada, Pennsylvania, and South Dakota – have presented a joint appeal, and we refer to them as "the states."

[22] The state commissions of Kansas and Vermont filed a separate appeal. Although both Kansas and Vermont challenge the 25% allocation, only Vermont maintains its challenge to the FCC's transitional support rules for rural carriers. *See infra* part III.A.6.c.i.

[23] *See Seventh Report and Order* § 3 ("We explicitly reconsider and repudiate any suggestion in the *First Report and Order* that federal support should be limited to 25 percent of the difference between the benchmark and the forward-looking cost estimates. . . . ").

when a state cannot by itself maintain reasonable comparability. *Seventh Report and Order* ¶ 34. This new framework is "a different regulation, containing on its face reasoning not previously articulated by the agency as its policy." *Center for Science in the Pub. Interest*, 727 F.2d at 1166. Therefore, we dismiss the challenges by all of the petitioners as moot.[24]

d. PROPERLY CONSULTING WITH THE JOINT BOARD BEFORE AMENDING JURISDICTIONAL SEPARATIONS RULES.

GTE raises an administrative procedural objection to the FCC's adoption of new jurisdictional separations rules[25] that propose to end existing high-cost fund support for non-rural carriers on January 1, 1999.[26] Instead of

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[24] Vermont invites us to review the *Seventh Report and Order's* interpretation of reasonable comparability in the context of that recent order's revised approach to allocating costs between the different states and between the state and federal funds. To the extent that Vermont's "reasonable comparability" arguments were based on a challenge to the 25% allocation, we dismiss its arguments as moot. To the extent its arguments focused on the alleged failure of the FCC to articulate a definition of "reasonable comparability," we would have to examine the merits of the *Seventh Report and Order*. As we explained, *supra* n. 16, we cannot review the merits of that order, because we lack jurisdiction over the merits of the new allocation methodology until it is transferred to this court by the District of Columbia Circuit.

[25] "Beginning January 1, 1999, non-rural carriers shall no longer receive support pursuant to this [program]." 47 C.F.R. § 36.601(c).

[26] This implementation date has now been delayed until January 1, 2000. *See Seventh Report and Order* ¶ 5.

arguing that the new rule is arbitrary and capricious, GTE claims that the agency failed properly to refer the matter to the Joint Board, in violation of 47 U.S.C. § 410(c), which states that "[t]he Commission shall refer any proceeding regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations . . . to a Federal-State Joint Board."

The FCC responds that it did make a general referral to the Joint Board in March 1996 and that the Joint Board subsequently recommended that the agency replace the existing support mechanisms for non-rural carriers with a new universal service system. The plan to replace the existing support mechanism, the FCC argues, requires a change in the method of jurisdictional separation, and by recommending the plan, the Joint Board had already considered the jurisdictional effects.[27]

GTE and the FCC disagree on the level of specificity needed to fulfill the Joint Board consultation requirement of § 410(c). GTE argues that simply identifying the broad subject of universal service reform did not raise the issue of altering the system that is used to shift costs in many high-cost areas to the interstate jurisdiction. In particular, GTE contends that the Joint Board failed to consider the

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[27] Jurisdictional separations rules are part of a process whereby it "may be determined what portion of an asset is employed to produce or deliver interstate as opposed to intrastate service." *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 356, 106 S.Ct. 1890, 90 L.Ed.2d 369 (1986). Section 410(c) requires the FCC to consult the Joint Board, but it does not "dictate how costs must be recovered. . . . " *See National Ass'n of Regulatory Util. Comm'rs v. FCC*, 737 F.2d 1095, 1112 n. 19 (D.C.Cir.1984).

amounts of the fund allocation between the interstate and intrastate jurisdictions when it considered the plan to implement a new support mechanism.

Although the FCC does not have to raise every possible detail in its referral to the Joint Board, it must show that the Joint Board was aware of the effects on the jurisdictional separations rules of replacing the existing high-cost support system. The plain language of the statute shows that any shift in the allocation of jurisdictional responsibility lies at the heart of § 410(c)'s consultation requirement.

The Joint Board was aware that replacing the existing high-cost support system will affect the jurisdictional separations rules. This is shown by the fact, for instance, that the Joint Board made a detailed discussion of the current jurisdictional separations rules, acknowledging that they "currently assign 25 percent of each LEC's loop costs to the interstate jurisdiction." *See* First Recommended Decision ¶ 188.

In discussing the comments submitted by affected parties, the Joint Board recognized that the jurisdictional separations rules are part of the old regime of "embedded" or "historical" costs. *See id.* ¶ 207. Thus, the Joint Board does seem to recognize that the jurisdictional separations rules are part of the old "embedded cost" system and were developed in the context of allocating the actual costs of developing the local and long-distance networks. By recommending replacing the historical cost system with a forward-looking "most efficient" cost model, the Joint Board must have considered that the jurisdictional separations rules no longer would apply in the same way.

Although no detailed discussion appears in the First Recommended Decision, the Joint Board's recognition that the jurisdictional separations rules would be affected by adopting a new cost model fulfills § 410(c)'s consultation requirement.[28]

2. Eligibility Requirements for Carriers Seeking Universal Service Support.

The states and intervenor Southwestern Bell ("SBC") challenge the FCC's reading of the Act's provisions governing eligibility requirements for carriers seeking universal service support. In general, they question the agency's interpretation of § 214(e) as too narrow and restrictive of the ability of state commissions to set their own criteria and exercise their own discretion over a carrier's eligibility.

a. Limiting the Criteria That State Commissions May Consider When Assessing a Carrier's Eligibility.

Section 214(e) governs the designation of carriers eligible to receive federal universal service support. Section 214(e)(1)(A) and (B) set out the eligibility requirements,

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[28] The FCC did not arbitrarily and capriciously fail to explain the reason for its amendment of rule 36.601(c). It stated that the new universal service mechanism will replace the old high-cost fund subsidies and that the change will occur on January 1, 1999 (later extended to July 1, 1999 and then to January 1, 2000). The agency's general explanations of the effect of the new support mechanism provide enough of a reason to survive GTE's attack.

and § 214(e)(2)[29] governs the designation of eligible carriers by state commissions.

In the Order, the FCC interpreted § 214(e)(2) in this way. With limited exceptions for rural areas, a state commission has no discretion when assessing a carrier's eligibility for federal support. If a carrier satisfies the terms of § 214(e)(1), a state commission *must* designate it as eligible. Thus, the FCC ruled that a state commission may not impose additional eligibility requirements on a carrier seeking universal service support in non-rural service areas. *See* Order ¶ 135. The agency does permit the states to impose service quality obligations on local carriers if those obligations are unrelated to a carrier's eligibility to receive federal universal service support. According to

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[29] The subsection reads:

> A State commission shall upon its own motion or upon request designate a common carrier that meets the requirements of paragraph (1) as an eligible telecommunications carrier for a service area designated by the State commission. Upon request and consistent with the public interest, convenience, and necessity, the State commission may, in the case of an area served by a rural telephone company, and shall, in the case of all other areas, designate more than one common carrier as an eligible telecommunications carrier for a service area designated by a State commission, so long as each additional requesting carrier meets the requirements of paragraph (1). Before designating an additional eligible telecommunications carrier for an area served by a rural telephone company, the State commission shall find that the designation is in the public interest.

the FCC, this interpretation "gives effect to the unambiguously expressed intent of Congress." *See Chevron*, 467 U.S. at 842-43, 104 S.Ct. 2778.

The states and SBC offer two lines of attack. First, they argue that the plain language of § 214(e)(2) does not support the FCC's blanket prohibition on additional state eligibility requirements. Second, they say that the FCC exceeded its jurisdictional authority, in violation of 47 U.S.C. § 152(b), by purporting to interfere with the states' regulation of intrastate service. Because we conclude that the agency erred in prohibiting the states from imposing additional eligibility requirements, we do not reach the states' jurisdictional challenges.

On the plain language front, the states argue that § 214(e)(2) does not unambiguously prohibit them from regulating carriers receiving federal universal support. Specifically, they contend that Congress did not mean to prohibit the states from imposing service quality standards on eligible carriers. According to the states, the language on which the FCC relies – "[a] State Commission shall upon its own motion or upon request designate a common carrier that meets the requirements of paragraph (1) as an eligible telecommunications carrier" – does not expressly circumscribe state authority to add additional eligibility requirements.

The agency's best hope for express authority for its action rests on the statute's use of the word "shall" in § 214(e)(2). Generally speaking, courts have read "shall" as a more direct statutory command than words such as

"should" and "may."[30] Though we agree that the use of the word "shall" indicates a congressional command, nothing in the statute indicates that this command prohibits states from imposing their own eligibility requirements. Instead, we read § 214(e)(2) as addressing *how many* carriers a state may designate for a given service area, and not how much discretion a state commission retains to impose eligibility standards.

The first sentence requires state commissions to designate at least one common carrier as eligible, but that carrier must still meet the eligibility requirements in § 214(e)(1). The second sentence then confers discretion on the states to designate more than one carrier in rural areas, while requiring them to designate eligible carriers in non-rural areas consistent with the "public interest" requirement. Nothing in the statute, under this reading of the plain language, speaks at all to whether the FCC may prevent state commissions from imposing additional criteria on eligible carriers.[31]

Thus, the FCC erred in prohibiting the states from imposing additional eligibility requirements on carriers otherwise eligible to receive federal universal service support. The plain language of the statute speaks to the

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[30] *See MCI Telecomm. Corp. v. FCC*, 765 F.2d 1186, 1191 (D.C.Cir.1985) (holding that "shall" is "the language of command").

[31] To be sure, if a state commission imposed such onerous eligibility requirements that no otherwise eligible carrier could receive designation, that state commission would probably run afoul of § 214(e)(2)'s mandate to "designate" a carrier or "designate more than one carrier."

question of *how many* carriers a state commission may designate, but nothing in the subsection prohibits the states from imposing their own eligibility requirements.[32] This reading makes sense in light of the states' historical role in ensuring service quality standards for local service. Therefore, we reverse that portion of the Order prohibiting the states from imposing any additional requirements when designating carriers as eligible for federal universal service support.

b. The Terms of Section 214(e)(5) Governing the Definition of Service Areas.

In their initial brief, the states argued that the FCC had impermissibly encroached on their exclusive authority to designate service areas for universal service support. The FCC, however, pointed out that ¶ 185 of the Order had only *encouraged* the states to make certain decisions[33] when designating service areas. The agency

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[32] Additionally, § 152(b) of Act instructs us to construe the Act to avoid giving the FCC jurisdiction over "charges, classifications, practices, services, facilities, or regulations for and in connection with intrastate communications services. . . ." 47 U.S.C. § 152(b). *See Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 376 n. 5, 106 S.Ct. 1890, 90 L.Ed.2d 369 (1986) ("[Section] 152(b) not only imposes jurisdictional limits on the power of a federal agency, but also, by stating that nothing in the Act shall be construed to extend FCC jurisdiction to intrastate service, provides its own rule of statutory construction."); *see also* discussion of "no disconnect" rule, *infra* part III.A.3.

[33] In order to promote competition, the FCC encourages states to adopt the existing study areas of ILECs as service areas

explicitly denies that the paragraph requires the states to follow its "encouragements." Thus, it appears that the states misinterpreted the FCC's intentions in ¶ 185 and that there is no issue left for us to address.

The states, however, continue to contest one aspect of the Order regarding the definition of service areas. The FCC maintains that it may establish a different definition of service areas for rural carriers, with the agreement of the states, without having to submit such a new definition first to the Joint Board. The states argue that the plain language of § 214(e)(5) allows the agency to act only "after taking into account recommendations of [the Joint Board]. . . . "

The FCC has two procedural responses and one substantive defense. Because we agree with the FCC that the states have no standing, we do not reach the FCC's other defenses.

The agency argues that the states have no standing to challenge its ruling, because the states have failed to show any harm.[34] After all, as the FCC points out, it must still garner the approval of each respective state before a

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for non-rural areas because it would create a significant barrier to entry. The FCC further encourages states to consider designating service areas that the ILECs have not traditionally served, this limiting the ILEC advantage over new entrants.

Order ¶ 185.

[34] We review the FCC's standing defense, like all constitutional questions, under a *de novo* standard of review. *See* 5 U.S.C. § 706 (stating that "a reviewing court shall decide all relevant questions of law [and] interpret constitutional and statutory provisions").

rural service area can be redefined. The states argue that they are harmed because the state members of the Joint Board are denied a chance to participate in the decision-making process, so the states are less able to coordinate with each other. They further contend that bypassing the Joint Board denied the states any meaningful participation in revising service area definitions for rural territories.

This claim is weak, because the states' independent ability to veto particular service areas seems to provide them with a substantial amount of "meaningful participation." This is unlike the situation in the cases the states rely on, in that the states here are not challenging a federal preemption order that threatens their sovereign authority. *See California v. FCC*, 75 F.3d 1350, 1361 (9th Cir.1996). Therefore, the states lack standing to challenge this portion of the Order.

c. Declining To Require Eligible Carriers To Offer Supported Services on an Unbundled Basis.

GTE argues that the FCC's failure to require carriers to "unbundle" their offerings when receiving universal service support violates the congressional intent expressed in § 214(e)(1) under *Chevron* step-one. "Bundling" refers to a carrier's practice of offering different services together as one package. For instance, a carrier might offer basic phone service as part of a package that includes call-waiting and voicemail.

GTE fears that a new carrier could "cherry pick" high-profit customers by offering only bundled local telephone service packages. Because the intended beneficiaries of universal service are, by definition, less able to afford even basic service, offering expensive bundled packages will allow new carriers to steal wealthier, low-cost customers while leaving ILEC's such as GTE to provide service to everyone else. GTE reasons that Congress, by requiring carriers receiving federal universal service support to advertise the availability of its supported services, intended to require new carriers to participate in universal service – an intent that would be thwarted by allowing the new carriers to offer bundled services.

The FCC responds that the plain language of the statute is satisfied as long as a carrier offers "services that are supported by Federal universal service mechanisms." 47 U.S.C. 214(e)(1)(A). Except for the advertising requirement, the statute makes no mention of "bundling" or other eligibility criteria. In fact, the FCC argues that because of the exclusive grant of eligibility authority conferred on the states by § 214(e)(2), it *cannot* impose additional eligibility criteria. Because the statute is silent on the question of bundling, and because the statute seems to prohibit further eligibility criteria, the agency asks us to give deference to its interpretation of § 214(e) under *Chevron* step-two.

We agree that the statute's plain language does not reveal Congress's unambiguous intent. It is not evident, however, that the FCC's interpretation of the statute meets even the minimum level of reasonability required in step-two review.

Section 214(e)(1) plainly requires carriers receiving universal service support to offer such supported services to as many customers as possible. Thus, an eligible carrier must offer such services "throughout the service area" and "advertise the availability of such services." This requirement makes sense in light of the new universal service program's goal of maintaining affordable service in a competitive local market. Allowing bundling, however, would completely undermine the goal of the first two requirements, because a carrier could qualify for universal service support by simply offering and then advertising expensive, bundled services to low-income customers who cannot afford it.

The FCC suggests that GTE's problems stem not from bundling but from state-imposed "carrier of last resort" ("COLR") requirements, which prohibit ILEC's such as GTE from disconnecting low-profit consumers and leave ILEC's vulnerable to outside competition. But the elimination of COLR requirements would only further undermine the goal of making basic services available to low income consumers and those in "rural, insular, and high cost areas." *See* 47 U.S.C. § 254(b)(3). This again would violate the express intent of the universal service program. Without a better explanation for its unreasonable interpretation, we would be inclined to find the FCC's implementation "arbitrary and capricious and manifestly contrary to the statute." *See Chevron*, 467 U.S. at 844, 104 S.Ct. 2778.

Fortunately, the agency also has explained that "only an eligible carrier that succeeds in attracting and/or maintaining a customer base to whom it provides universal service will receive universal service support." Order

¶ 138. Therefore, it reasons that if offering only bundled services would price low-income customers out of the market, the carrier offering bundled services would eventually lose universal service support. Thus, the FCC can avoid the problem of providing universal service support to carriers that do not serve high-cost customers for which the support is intended. This explanation supports the FCC's claim that its decision to allow bundling is reasonable under *Chevron* step-two review.

Though the decision is a close one, we conclude that the FCC's refusal to require eligible carriers to provide unbundled services is neither "arbitrary, capricious," nor "manifestly contrary to the statute." *See Chevron*, 467 U.S. at 844, 104 S.Ct. 2778. Because the agency will prevent companies from using bundling to receive federal support while avoiding high-cost customers, we do not find its interpretation "so implausible that it could not be ascribed to a difference in view or the product of agency expertise." *Motor Vehicle Mfrs.' Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43, 103 S.Ct. 2856, 77 L.Ed.2d 443 (1983).

3. Authority To Prohibit Carriers from Disconnecting Local Service to Low-income Consumers Who Fail To Pay Toll Charges.

Bell Atlantic and the states challenge the FCC's adoption of a regulation[35] prohibiting carriers receiving universal service support from disconnecting Lifeline

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[35] 47 C.F.R. § 54.401(b).

services[36] from low-income consumers who have failed to pay toll charges. *See* Order ¶ 390. The petitioners charge that the "no disconnect" rule exceeds the agency's jurisdictional authority under § 2(b) of the 1934 Act,[37] which prohibits FCC regulation of intrastate telecommunications service. Because the plain language of the statute expresses Congress's unambiguous intent, we review the agency's interpretation under *Chevron* step-one.

The agency has three responses. First, it argues that § 2(b) does not apply where Congress has given the FCC an "unambiguous or straightforward" grant of authority. *See Louisiana Pub. Serv. Comm'n*, 476 U.S. at 377, 106 S.Ct. 1890. The agency argues that Congress granted such express authority in § 254(b)(3), which directs the FCC to base its policies on the principle that "low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services. . . . "

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[36] The Lifeline program refers to the FCC's efforts to expand telephone services to qualifying low-income subscribers. The agency defines Lifeline services to include single-party service, voice-grade access to the public switched telephone network, BTMF or its functional digital equivalent, access to directory assistance, and toll-limitation services. *See* Order ¶ 390.

[37] "[N]othing in this subchapter shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier. . . . " 47 U.S.C. § 152(b) (as amended).

As we have discussed, § 254(b) identifies seven principles the FCC should consider in developing its policies; it hardly constitutes a series of specific statutory commands. Indeed, we have avoided relying on the aspirational language in § 254(b) to bind the FCC to adopt certain cost methodologies for calculating universal service support.[38]

Just as we declined to read § 254(b) as an inexorable statutory command against the FCC, we decline to read it as a grant of plenary power overriding other portions of the Act. The agency has no "unambiguous or straightforward" grant of authority to override the limits set by § 2(b), and, accordingly, it has no jurisdiction to adopt the "no disconnect" rule on the basis of the vague, general language of § 254(b)(3).[39]

Second, the FCC contends that the petitioners' jurisdictional challenge is inapposite because the "no disconnect" rule does not purport to regulate intrastate service, but merely prevents the disconnection of interstate service (and, as a consequence, of intrastate service) for failure to pay toll charges.[40] As Bell Atlantic rightly

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[38] *See supra* part III.A.1.a.i.

[39] The SBC intervenors challenge a related FCC rule prohibiting the practice of requiring deposits from customers initiating service with toll-blocking for interstate service. Unfortunately for SBC, none of the petitioners on this issue (the states and Bell Atlantic) raised a challenge to this similar but separate rule in the FCC proceeding. Therefore, we cannot consider it on appeal. *See United Gas Pipe Line Co. v. FERC*, 824 F.2d 417, 437 (5th Cir.1987).

[40] Bell Atlantic argues that the FCC has waived this argument on appeal. We do not agree. The FCC's brief states

responds, however, the "no disconnect" rule is a "regulation," because it dictates the circumstances under which local service must be maintained. Therefore, the FCC, by issuing the rule, has acted "with respect to" and "in connection with" intrastate service within the meaning of § 2(b).

The FCC points out that even if the "no disconnect" rule is a "regulation" within the meaning of § 2(b), courts have sustained agency jurisdiction over similar rules under the "impossibility" exception. In *North Carolina Utils. Comm'n v. FCC*, 552 F.2d 1036 (4th Cir.1977), the court upheld FCC regulations permitting local subscribers to connect their telephones to the local loop to make interstate calls. North Carolina previously had required subscribers to use leased telephones and argued that § 2(b) prevented FCC intervention because the vast majority of these calls were intrastate. The court rejected this argument, holding that "the FCC has jurisdiction to prescribe the conditions under which terminal equipment may be interconnected with the interstate telephone line network." *Id.* at 1048.

Essentially, the FCC asks us to find that the "no disconnect" rule, aimed at regulating interstate service, is impossible to separate from intrastate service. In similar

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that the "no disconnect" rule "does not purport to regulate intrastate service . . . but merely to prevent the disconnection of service (including interstate access service) to customers who have failed to pay toll charges." Though weak, this statement preserves the FCC's attempt to exceed its jurisdictional boundaries on the ground that it cannot regulate an interstate matter without also regulating an intrastate matter.

cases, the District of Columbia Circuit has permitted the FCC to intervene in relatively localized service issues[41] and has developed a useful framework for analyzing what the petitioners refer to as the "impossibility" exception to § 2(b). *See Public Serv. Comm'n v. FCC ("Maryland PSC")*, 909 F.2d 1510, 1515 (D.C.Cir.1990).

To permit the FCC to preempt state regulation of whether to cut off low-income subscribers, that circuit requires the agency to show that "(1) the matter to be regulated has both interstate and intrastate aspects; (2) FCC preemption is necessary to protect a valid federal regulatory objective; and (3) state regulation would negate the exercise by the FCC of its own lawful authority because regulation of the interstate aspects of the matter cannot be unbundled from regulation of intrastate aspects." *Maryland PSC*, 909 F.2d at 1515 (internal quotations and citations omitted). This framework creates a properly narrow exception to § 2(b) that allows the FCC to preempt state regulation only when it has shown it cannot carry out its authorized federal objectives without encroaching on state autonomy.

Applying this framework to the "no disconnect" rule, we agree with Bell Atlantic that the FCC has failed to show why allowing the states to control disconnections from local service would "negate the exercise of the FCC's lawful authority. . . . " As Bell Atlantic points out,

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[41] *See, e.g., Public Util. Comm'n v. FCC*, 886 F.2d 1325 (D.C.Cir.1989); *Illinois Bell Tel. Co. v. FCC*, 883 F.2d 104 (D.C.Cir.1989); *National Ass'n of Regulatory Util. Comm'rs v. FCC*, 880 F.2d 422 (D.C.Cir.1989).

the agency offered only a brief explanation of what lawfully authorized federal objectives are being served by the "no disconnect" rule and why it is necessary to preempt local authority to achieve these objectives.

In the Order, the FCC simply states that the "no disconnect" rule advances its goal of increasing subscribership and that it will improve the competitiveness of the market for billing and collection of toll charges. *See* Order ¶¶ 390-391. But the agency has not adequately explained, in either its brief or its Order, why these goals would be "negated" by allowing the states to control disconnection of local subscribers. In contrast to what occurred in *Maryland PSC*, where the court allowed the FCC to assert jurisdiction to prevent ILEC's from shifting local costs to interstate consumers, the FCC has offered no similar explanation of how protecting interstate service *requires* imposition of a "no disconnect" rule. Therefore, we decline to allow the agency to assert jurisdiction over the disconnection of local service based on the impossibility exception.

Finally, the FCC argues that in the wake of *Iowa Utilities*, it has jurisdiction over all areas, including intrastate matters, to which the Act applies. In *Iowa Utilities*, the Court rejected jurisdictional challenges to the portions of the FCC's *Local Competition Order* implementing §§ 251 and 252 of the Act, which govern the interconnection of new local service carriers with the ILEC's and establish procedures for negotiating, arbitrating, and approving any interconnection agreements. As in the instant case, petitioners challenged the FCC's jurisdiction to implement the Act, arguing that much of the authority to enforce the provisions (§§ 251 and 252) remain with the

state commissions by virtue of § 2(b). Specifically, they contended that the Act gives the FCC jurisdiction over intrastate matters only when the statute explicitly applies to intrastate services and specifically confers agency jurisdiction over intrastate services.

The Court brushed aside these attempts to raise the § 2(b) jurisdictional fence and squarely held that " § 201(b)[42] *explicitly* gives the FCC jurisdiction to make rules governing matters to which the 1996 Act applies." *Iowa Utilities*, 119 S.Ct. at 730. Though § 2(b)'s language stating that "nothing in this Act shall be construed to apply or to give the Commission jurisdiction" implies that FCC jurisdiction does not always follow where the Act applies, the Court held that "the term 'apply' limits the substantive reach of the statute . . . and the phrase 'or Commission jurisdiction' limits . . . the FCC's *ancillary* jurisdiction." *Id.* at 731. Relying on this holding, the FCC argues that because § 254 *applies* to intrastate as well as interstate matters, § 201(b) confers the necessary jurisdiction to implement the "no disconnect" rule.

Though the Court's broad language seems to support the FCC's position, Bell Atlantic finds comfort in the Court's preservation of *Louisiana PSC*. In reconciling its holding with *Louisiana PSC*, the Court held that the FCC must show that the meaning of a statutory provision *applies* to intrastate matters in an "unambiguous and straightforward" manner as "to override the command of § 2(b)." *Iowa Utilities*, 119 S.Ct. at 731 (quoting *Louisiana*

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[42] "The Commission may prescribe such rules and regulations as may be necessary in the public interest to carry out the provisions of this Act." 47 U.S.C. § 201(b).

PSC, 476 U.S. at 377, 106 S.Ct. 1890). If the agency fails in this initial task, it cannot use its normally broad regulatory authority to assert what is now only *ancillary* jurisdiction because of the still-intact jurisdictional fence created by § 2(b). *See id.* Therefore, after *Iowa Utilities*, § 2(b) still serves as (1) a rule of statutory construction[43] requiring the FCC to find unambiguous statutory authority *applying* to intrastate matters and (2) a jurisdictional barrier restricting the agency from using its plenary authority to assert *ancillary* jurisdiction by "taking intrastate action solely because it further[s] an interstate goal." *See Iowa Utilities*, 119 S.Ct. at 731 (citing *Louisiana PSC*, 476 U.S. at 374, 106 S.Ct. 1890).

The question is whether § 254 does indeed "apply" to intrastate matters in a sufficiently "unambiguous" manner. Without such a finding, *Iowa Utilities* flatly holds that the FCC cannot use its plenary authority to assert ancillary jurisdiction.

Unfortunately, *Iowa Utilities* provides little guidance for resolving the question whether § 254 applies to intrastate services. For the Supreme Court, "the question . . . is not whether the Federal Government has taken the regulation of local telecommunications competition away from the States. With regard to the matters addressed by the 1996 Act, it unquestionably has." *Iowa Utilities*, 119

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[43] *Accord Louisiana PSC*, 476 U.S. at 376 n. 5, 106 S.Ct. 1890 ("[Section] 152(b) not only imposes jurisdictional limits on the power of a federal agency, but also, by stating that nothing in the Act shall be construed to extend FCC jurisdiction to intrastate service, provides its own rule of statutory construction.")

S.Ct. at 730 n. 6. The Court did not further explain why it felt §§ 251 and 252 "unquestionably" applied to intrastate matters.

The FCC bases its contention that § 254 plainly applies to intrastate as well as interstate matters on § 254(b)(3),(c), and (j). According to the agency, § 254(b)(3) applies to intrastate service by stating that "low income consumers . . . should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services."

The use of the word "including," the FCC argues, indicates that the object of § 254 is to provide access to more than just interexchange services. Furthermore, § 254(c) instructs the agency to consider, in the process of establishing what constitutes universal service, whether such services "have . . . been subscribed to by a substantial majority of residential customers." Finally, § 254(j) specifically preserves the Lifeline Assistance program, which has always provided subsidies for both intrastate and interstate services.

We have already discussed our reluctance to rely on the aspirational language of § 254(b).[44] Moreover, the phrase "including interexchange carriers" cannot be said unambiguously to mean that § 254 applies to local services, and § 254(c)'s mention of a "majority of residential customers" is far from straightforward. Neither is there much guidance from § 254(j), which specifically protects the Lifeline Assistance program from being affected by

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[44] *See supra* part III.A.3.

any other part of § 254 but does not in any way clarify to what degree § 254 applies to intrastate universal service.

Instead, there is substantial support in the statute for a dual regulatory structure in the administration of the universal service program. Section 254(d) specifically instructs interstate carriers to contribute to the FCC's universal service mechanisms, while § 254(f) instructs intrastate carriers to contribute to the states' individual universal service mechanisms. This section contains the only discussion of intrastate universal service mechanisms and directs intrastate carriers to report to the states rather than to the FCC.

In light of *Iowa Utilities* and *Louisiana PSC*, therefore, we conclude that, "while it is, no doubt, possible to find some support in the broad language of the section for [the FCC's] position, we do not find the meaning of the section so unambiguous or straightforward as to override the command of § 152(b)." *Louisiana PSC*, 476 U.S. at 377, 106 S.Ct. 1890. Unlike §§ 251 and 252, which were solely concerned with intrastate issues (i.e., interconnection of new entrants into the local telephone market), § 254 applies to both interstate and intrastate services. It does so, however, only to the extent that it gives exclusive authority over intrastate contributions to the state commissions. We find it incongruous to use this explicit limitation on FCC authority as the hook to provide it with jurisdiction.

Therefore, the FCC exceeded its jurisdiction when it imposed the "no disconnect" rule. Because there is no express grant of statutory authority, a proper showing of "impossibility," or a persuasive explanation of how § 254

applies to intrastate service, we reverse, for want of agency jurisdiction, those portions of the Order implementing the "no disconnect" rule.

4. Recovery of Universal Service Contributions.

a. - Requiring Incumbents To Recover Contributions Through Access Charges.

GTE and the FCC again wrangle over the meaning of "explicit" in their dispute regarding the rule requiring most ILEC's to recover their universal service contributions through access charges. GTE contends that the rule violates § 254(e)'s command that any support for universal service be "explicit," because recovering contributions through increased access charges is a form of implicit subsidy.

GTE argues that the rule unfairly disadvantages ILEC's because, unlike their potential new competitors, they cannot recover their universal service contributions through explicit charges on their end-users, but, instead, are required by the FCC to increase their access charges on long-distance service providers. Though they do not necessarily lose out in terms of amounts recovered, GTE fears that this recovery method will put them at a competitive disadvantage because, instead of than [sic] seeing the costs of universal service on his bill as an explicit surcharge, an ILEC consumer will pay for the costs of universal service through higher rates.

The FCC advances a different understanding of "explicit." "Regardless of how carriers recover their contributions, the FCC's universal service system 'satisfies

the statutory requirement that support be explicit' by requiring each carrier to contribute a specific percentage of its end user revenues" (quoting Order ¶ 854). As long as carriers know exactly how much they are contributing to the support mechanisms, the subsidies are explicit.

The statute provides little guidance on whether "explicit" means "explicit to the consumer" (as urged by GTE) or "explicit to the carrier" (as urged by the FCC). The statute does state, however, that all universal service *support* should be "explicit." We read "explicit" to mean the opposite of "implicit." *See* § 254(e).

By forcing GTE to recover its universal service contributions from its access charges, the FCC's interpretation maintains an implicit subsidy for ILEC's such as GTE. In fact, requiring carriers to recover their contributions from access charges on interstate calls shifts the costs of intrastate universal service to the interstate jurisdiction. These are precisely the sorts of implicit subsidies currently used by the FCC in its DAM weighting program. *See* Order ¶ 212 (discussing rules that permit small LEC's to recover costs for intrastate services from interstate access charges).

We are convinced that the plain language of § 254(e) does not permit the FCC to maintain *any* implicit subsidies for universal service support. Therefore, we will not afford the FCC any *Chevron* step-two deference in light of this unambiguous Congressional intent. Because the agency continues to require implicit subsidies for ILEC's in violation of a plain, direct statutory command,

we reverse its decision to require ILEC's to recover universal service contributions from their interstate access charges.

b. Requiring Interstate Carriers To Reduce Interstate Access Charges by the Amount of Federal High-cost Support They Receive Under the New Universal Service System.

The states contest an aspect of the Order's effect on interstate access charges, arguing that the requirement that carriers reduce their interstate access charges by the amount of direct federal high-cost support they receive will leave insufficient funds for intrastate universal service. The states make two unconvincing plain-language arguments. First, they point to § 254(b)(5)'s language about "specific, predictable and sufficient" mechanisms to "preserve and advance universal service." As we have observed, § 254(b) identifies a set of principles and does not lay out any specific commands for the FCC. Even § 254(e), which is framed as a direct, statutory command, is ambiguous as to what constitutes "sufficient" support. Therefore, we do not consider the language an expression of Congress's "unambiguous intent" allowing *Chevron* step-one review, and we review its interpretation for reasonability under *Chevron* step-two.

The states argue that § 254(e) does not permit the application of federal universal service funds for the interstate jurisdiction. In essence, they seek to preserve *state* universal service support by reading the statute to require all high-cost support to remain intrastate. Though

this might make compelling policy, nothing in the plain language of § 254(e)[45] unequivocally establishes the states' right to all of the federal universal support funds. The statutory language is at best ambiguous as to Congress's intent, which, under *Chevron* step-two, leaves it to the FCC's reasonable interpretation.

The FCC has offered good reason to believe that its new explicit support through direct subsidies will replace the amounts lost through the reduction of access charges. *See* Report to Congress ¶ 230. To be sure, the states and intervenor NASUCA[46] make a plausible argument that ILEC's will receive less under the new plan than they did through implicit subsidies. As we have determined, however, because the FCC has offered reasonable explanations of why it thinks the funds will still be "sufficient" to support high-cost areas, we defer to the agency's judgment of what is "sufficient."

Under the agency's new universal service plan, it is possible that the states will receive less support for intrastate universal service costs than they did under the old plan. While this may seem unfair as a matter of policy, the states have failed to show that the FCC's interpretation, which may possibly result in a reduction of their level of support, is "arbitrary, capricious, or manifestly contrary to the statute." *Chevron*, 467 U.S. at 844, 104 S.Ct. 2778.

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[45] "A carrier that receives such support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."

[46] National Association of State Utility Consumer Advocates.

5. CONTRIBUTIONS.

a. REQUIRING CMRS CARRIERS TO CONTRIBUTE TO THE FEDERAL UNIVERSAL SERVICE FUND.[47]

Celpage Inc., a paging carrier, and intervenors representing a number of wireless telecommunications companies (referred to in general as commercial mobile radio service or "CMRS" providers), challenge the FCC's decision to subject them to the universal service support scheme. Celpage raises a number of constitutional and statutory challenges to the decision to require their contributions to the universal service fund. Specifically, Celpage attacks the agency's universal service contribution requirement as an unconstitutional tax, a violation of equal protection, and an uncompensated taking. Additionally, Celpage charges that the FCC's action violates § 254's plain language, is arbitrary and capricious, and does not meet the agency's own principle of competitive neutrality.

i. CONSTITUTIONAL CHALLENGES.

(a). UNCONSTITUTIONAL TAX.

There are two ways in which the universal service contribution requirement for paging carriers could constitute an unconstitutional tax. First, the FCC's application

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[47] Intervenor American Cable Television Association challenges the FCC for failing to meet the requirements of the Regulatory Flexibility Act before promulgating the Order. None of the petitioners raises this argument, nor does the FCC respond to it, and therefore we do not consider it. *See* discussion of MCI's intervenor argument, *infra* part III.A.6.b.

of the universal service requirement to paging carriers such as Celpage might be an unconstitutional delegation of Congress's exclusive taxing power under the Taxing Clause.[48] Alternatively, because the Act originated in the Senate,[49] its requirement of universal service contributions from paging carriers might violate the Origination Clause's requirement that all "[b]ills for raising [r]evenue originate in the House of Representatives"[50]

Despite their similarities, the Taxing Clause and Origination Clause challenges to the universal service contribution system represent separate lines of analysis.[51] In its initial brief, however, Celpage raises only the Origination Clause challenge and does not raise a Taxing Clause claim until its reply brief. Therefore, we will not

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[48] U.S. CONST., art. I, § 8, cl. 1 ("The Congress shall have Power to lay and collect Taxes. . . . ").

[49] *See* Telecommunications Act of 1996, Pub.L. No. 104-104, 110 Stat. 56 (1996) (enacting S. 652).

[50] U.S. CONST., art. I, § 7, cl. 1 ("All Bills for Raising Revenue shall originate in the House of Representatives.")

[51] The Taxing Clause analysis focuses on whether the assessment is a tax or a fee. This question is usually resolved based on whether the revenues are used to primarily defray the expenses of regulating the act. *See National Cable Television Ass'n v. United States*, 415 U.S. 336, 340, 94 S.Ct. 1146, 39 L.Ed.2d 370 (1974). If it is a tax, then courts will ask whether it has been properly delegated. *Id.* On the other hand, the Origination Clause analysis asks whether (1) the revenues generated from the assessment are for general revenues or for a particular program and (2) there is a connection between the payors and the beneficiaries of the program. *See Munoz-Flores*, 495 U.S. at 397, 110 S.Ct. 1964. *See infra* part III.B.1.c. n.83.

consider it,[52] and we focus our efforts on Celpage's claim that the universal service contribution requirement, as applied to paging carriers, is a violation of the Origination Clause.[53]

Unfortunately for Celpage, its Origination Clause claim cannot survive *United States v. Munoz-Flores*, 495 U.S. 385, 398, 110 S.Ct. 1964, 109 L.Ed.2d 384 (1990). There, the Court refused to find that a special assessment on certain federal criminals for a "crime victim's" fund is a tax, because "a statute that creates a particular governmental program and that raises revenue to support that program . . . is not a 'Bil[l] for raising Revenue' within the meaning of the Origination Clause." *Id.*

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[52] Generally, we do not consider arguments raised for the first time in a reply brief. *See* FED. R.APP. P. 28(c). Even if Celpage's Taxing Clause argument were properly before us, we find no basis for reversal. As applied to paging carriers, the universal service contribution qualifies as a fee because it is a payment in support of a service (managing and regulating the public telecommunications network) that confers special benefits on the payees. *See National Cable*, 415 U.S. at 340, 94 S.Ct. 1146. *Cf. Rural Tele. Coalition v. FCC*, 838 F.2d 1307, 1314 (D.C.Cir.1988) (upholding universal service contributions as a fee supporting allocations between interstate and intrastate jurisdictions).

[53] The Supreme Court has squarely held that Origination Clause challenges are subject to judicial review and do not fall under the political question doctrine. "A law passed in violation of the Origination Clause would thus be no more immune from judicial scrutiny because it was passed by both Houses and signed by the President than would a law passed in violation of the First Amendment." *Munoz-Flores*, 495 U.S. at 397, 110 S.Ct. 1964.

Celpage points out that the Congressional Budget Office has treated universal service fund contributions as federal revenues. But how the government classifies a program for accounting purposes does not resolve whether the funds are used for a specific program or for general revenues. Indeed, the Court in *Munoz-Flores* upheld the special assessment even though the excess money collected was deposited in the Treasury. Instead of looking at accounting designations, *Munoz-Flores* teaches us (1) to determine whether the funds are "part of a particular program to provide money for that program. . . . " and (2) to establish a connection between the payors and the beneficiaries. *Munoz-Flores*, 495 U.S. at 399, 400 n. 7, 110 S.Ct. 1964.

With one exception,[54] universal service contributions are part of a particular program supporting the expansion of, and increased access to, the public institutional telecommunications network. *See* Order ¶ 8. Each paging carrier directly benefits from a larger and larger network and, with that in mind, Congress designed the universal service scheme to exact payments from those companies benefiting from the provision of universal service.[55] This

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[54] *See* discussion of § 254(h) support for internet services, *infra* part III.B.1. Unlike the circumstance in that case, the situation here is that of a telecommunications service provider's (a paging carrier's) being required to support the maintenance of a large telecommunications network.

[55] *See* § 254(d) ("Every telecommunications carrier that provides interstate telecommunications services shall contribute . . . to the . . . mechanisms established by the Commission to preserve and advance universal service."); § 254(f) ("Every telecommunications carrier that provides intrastate telecommunications services shall contribute. . . . ").

design prevents the sums being used to support the universal service program from being classified as "revenue" within the meaning of the Origination Clause.

Paging carriers are uniquely dependent on a widespread telecommunications network for the maintenance and expansion of their business. *See* Order ¶ 82. As in *Munoz-Flores*, the challenged assessment targets a group "to which some part of the expenses" of sustaining the universal service program "can fairly be attributed." *See Munoz-Flores*, 495 U.S. at 400 n. 7, 110 S.Ct. 1964. Therefore, the application of the universal service contribution requirement to paging carriers does not transform the Act into a "bill for raising revenue" in violation of the Origination Clause.[56]

(b). Equal Protection.

To invalidate the FCC's actions on equal protection grounds, we must find that there is no "basis for the action that bears a debatably rational relationship to a conceivable legitimate governmental end." *See Reid v.*

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[56] The *Munoz-Flores* Court does not discuss in great detail the importance, in Origination Clause analysis, of some kind of relationship between the payors and the beneficiaries. Still, it makes sense that the Court would insist on some link, because an assessment on one group for the benefit of a completely unrelated group is how courts have distinguished taxes raised for general federal outlays from fees raised for specific programs. Otherwise, Congress could *always* avoid the Origination Clause requirement because, in theory, all revenue is raised to fund some "particular program." Thus, courts must establish *some* relationship between the payors and the beneficiaries to avoid the strictures of the Origination Clause.

Rolling Fork Pub. Util. Dist., 979 F.2d 1084, 1087 (5th Cir.1992). This is a tough burden, and Celpage does not come close. Celpage argues there can be no rational reason to include paging carriers in the universal service contribution system, because its contributions will support services that do not benefit Celpage. But the FCC has offered a reasonable proposition: Paging carriers such as Celpage benefit from a larger and more universal public network system, because it increases the number of potential locations for paging use. Even if this proposition is wrong, as Celpage suggests, it certainly meets the very low "debatably rational" test.[57]

(c). TAKING.

Celpage advances an unconvincing takings claim. As an initial matter, a takings claim is not ripe until a claimant has unsuccessfully sought compensation from the state.[58] Celpage does not allege that it has used any of the FCC's administrative procedures to petition for compensation or that such procedures are so inadequate as to make resort to these procedures futile. "To violate the [takings] clause, the state must not only take someone's

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[57] *See Reid*, 979 F.2d at 1087 (5th Cir.1992) (stating that a "decision of a governmental body does not violate equal protection guarantees if there is any basis for the action that bears a debatably rational relationship to a conceivable legitimate governmental end").

[58] *See Williamson County Regional Planning Comm'n v. Hamilton Bank*, 473 U.S. 172, 193, 105 S.Ct. 3108, 87 L.Ed.2d 126 (1985).

property but also deny him compensation." *Samaad v. City of Dallas*, 940 F.2d 925, 934 (5th Cir.1991).

As we did in the case of GTE's challenge to the forward-looking cost methodology, we reject Celpage's takings claim as not ripe for judicial review.[59]

ii. Other Challenges.

Celpage attacks the FCC's interpretation of the "equitable and nondiscriminatory" language in § 254(b)(4). To be truly equitable, Celpage asserts, the agency should not treat all carriers in the same way for purposes of the universal service contribution system. Additionally, Celpage accuses the agency of failing to consider evidence of congressional intent, the record evidence, and other evidence of why paging carriers should not be included in the universal service contribution system.

The FCC has successfully dispensed with the plain language challenge. First, as we have explained, the "equitable and nondiscriminatory" language in § 254(b)

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[59] Even if we considered Celpage's takings claim, it would fail to demonstrate how its claim comports with the three factors the Supreme Court has established to analyze a regulatory takings claim: (1) the economic impact of the regulation on the claimant; (2) the extent to which the regulation has interfered with distinct investment-backed expectations; and (3) the character of the governmental action. *See Connolly v. Pension Benefit Guar. Corp.*, 475 U.S. 211, 225, 106 S.Ct. 1018, 89 L.Ed.2d 166 (1986). In particular, Celpage has failed to offer reasonably specific predictions of the size and scale of this taking, thereby failing to show the extent to which the regulation has interfered with its distinct investment-backed expectations.

acts as only one of seven guiding principles for FCC rulemaking. *See supra* part III.A.1.a.i. That subsection also instructs the agency that "*all providers* of telecommunications services should make an equitable and non-discriminatory contribution" to universal service. (Emphasis added.) The language of § 254(b) directs us to give the FCC, in addition to the usual *Chevron* deference, discretion here to fashion a policy that is guided by both of these principles.

Celpage also challenges the FCC's interpretation as arbitrary and capricious under the APA because it is not supported by the record, and the agency has provided no reason why its decision should be made in the face of contrary record evidence. Specifically, Celpage says that the FCC failed to consider *ex parte* statements by legislators during the rulemaking proceedings urging it to exclude CMRS carriers from the universal service contribution system. Additionally, Celpage points to evidence in the record supporting its position and claims the FCC failed to consider it.

To achieve reversal under the APA's arbitrary and capricious standard, Celpage must show that the FCC failed to "articulate[ ] a rational relationship between the facts found and the choice made. . . . " *Harris*, 19 F.3d at 1096. A reviewing court tries "to determine whether the decision was based on a consideration of relevant factors. . . . " *Louisiana v. Verity*, 853 F.2d 322, 327 (5th Cir.1988).

The record does not show that the FCC failed to consider the counter-arguments proffered by the CMRS providers and their allies. The agency did take note of

letters from Congress on behalf of CMRS providers and from other legislators taking the opposite position. *See* Report to Congress ¶ 129 & n.301. Moreover, the letters on both sides have limited persuasiveness, because they are simply "post-passage remarks" that " 'represent only the personal views of these legislators' " and "cannot serve to the change the legislative intent of Congress expressed before the Act's passage." *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 132, 95 S.Ct. 335, 42 L.Ed.2d 320 (1974) (quoting *National Woodwork Mfrs. Ass'n v. NLRB*, 386 U.S. 612, 639 n. 34, 87 S.Ct. 1250, 18 L.Ed.2d 357 (1967)).

The FCC offered a reasonable justification for including CMRS providers – this time relying on statutory language, the Joint Board recommendation, and the reasonable view that paging carriers do receive benefits from the universal service system. Accordingly, the agency's interpretation may not fairly be described as "arbitrary and capricious" under the APA.[60]

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[60] Celpage also challenges the FCC's ruling for violating its own principle of "competitive neutrality." Because this term has been developed by the FCC through regulation rather than through interpretation of the statute, we should give the agency broad deference in applying this principle, and we can reverse only if we find the FCC's actions "arbitrary, capricious or manifestly contrary to the statute." *Chevron*, 467 U.S. at 844, 104 S.Ct. 2778. The FCC's decision to require paging operators to contribute to the support of a network through which their business operates is not so irrational or arbitrary as to merit reversal.

iii. Implementing Universal Service Assessment Requirements.

Celpage and the CMRS Providers challenge the FCC's rules and procedures for assessing contributions in the form of the Universal Service Worksheet. Specifically, Celpage attacks the worksheet for failing to distinguish between billed revenues and collected revenues for purposes of calculating universal service contributions. The CMRS Providers complain that the FCC's failure to provide guidance on how to adjust for the different nature of CMRS revenues makes the assessment system unconstitutionally vague.

We do not reach the vagueness argument, because the FCC persuasively responds that these challenges are not yet ripe for judicial review, for the reason that the agency has made a "tentative decision."[61] Similar attacks on the Worksheet are currently pending before the agency as petitions for reconsideration.[62] Moreover, recognizing

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[61] *See Pub. Citizen Health Research v. Commissioner, Food & Drug Admin.*, 740 F.2d 21 (D.C.Cir.1984) (refusing to exercise judicial review over tentative agency actions absent excessive delay or extraordinary recalcitrance).

[62] On October 26, 1998, the FCC released an order and a further notice of proposed rulemaking on the question of how to assess wireless carriers' revenues. The agency made a tentative decision to provide wireless carriers with interim guidelines for how to approximate their percentage of interstate wireless revenues. Additionally, the agency sought comment on various proposals for a final guideline on such calculations and comment on the relationship of wireless communications providers to universal service. This order further supports the FCC's position that it has not yet made a final decision on how to handle these issues.

the difficulties that the Worksheet raises, the FCC has already granted CMRS providers interim relief by allowing them to provide good-faith estimates of the figures required by the Worksheet.

Thus, the agency properly asks us to defer judicial review of its tentative decision until all administrative remedies are exhausted. In analogous situations, courts have postponed review "until relevant agency proceedings have been concluded [to] permit[ ] an administrative agency to develop a factual record, to apply its expertise to the record, and to avoid piecemeal appeals." *See Telecommunications Research & Action Ctr. v. FCC*, 750 F.2d 70, 79 (D.C.Cir.1984) (internal citations omitted).

iv. States' Collection of Universal Service Assessment from CMRS Carriers.

Celpage and the CMRS Providers make a convincing challenge in contesting the FCC's decision to permit states to impose universal service contribution requirements on CMRS providers. They argue that the plain language of 47 U.S.C. § 332(c)(3)(A) specifically preempts states from doing so. Additionally, the CMRS Providers contend that § 254(f)'s language, relied on by the FCC, does not reach CMRS providers, because they are interstate carriers.

(a) Plain Language of § 332(c)(3)(A).

Celpage and the CMRS Providers argue that in § 332(c)(3)(A), "Congress has spoken to the precise question at issue," the ability of states to assess CMRS

providers for universal service contributions. *See Chevron*, 467 U.S. at 842, 104 S.Ct. 2778. Therefore, they argue that the FCC's interpretation deserves no deference. The plain language of § 332(c)(3)(A) does seem to apply to the issue at hand:

> Notwithstanding sections 152(b) and 221(b) of this title, no State or local government shall have any authority to regulate the entry of or the rates charged by any commercial mobile service or any private mobile service, except that this paragraph shall not prohibit a State from regulating the other terms and conditions of commercial mobile services. Nothing in this subparagraph shall exempt providers of commercial mobile services (where such services are a substitute for land line telephone exchange service for a substantial portion of the communications within such State) from requirements imposed by a State commission on all providers of telecommunications services necessary to ensure the universal availability of telecommunications service at affordable rates.

Before we discuss the differing interpretations of the statute, we must decide on the proper standard of review. The Tenth Circuit recently reviewed the FCC's interpretation of this section under the second step of *Chevron*, because the statute does not expressly state how we should read § 332(c)(3)(A) in relation to § 254(f). *See Sprint Spectrum v. State Corp. Com'n of Kansas*, 149 F.3d 1058, 1061 (10th Cir.1998). This standard of review is inappropriate, however, because it would allow the FCC to receive *Chevron* deference in almost every situation in which two sections of a statute must be read together. Indeed, the Act does contain a specific rule of statutory

construction in § 601(c)(1), *reprinted in* 47 U.S.C. § 152 (Addendum A-1): "This Act and the amendments made by this Act shall not be construed to modify, impair or supersede Federal, State or local law unless expressly provided in such Act or Amendments."

Thus, we disagree with the *Sprint* court that the lack of a specific provision discussing the relation between §§ 332(c)(3)(A) and 254(f) automatically triggers *Chevron* deference. To the contrary, § 601(c)(1) gives us explicit instruction to read § 254(f) ("federal law") as not conflicting with § 332(c)(3)(A). Therefore, we conduct a *Chevron* step-one review and try to search out the statute's plain meaning.

Celpage and the CMRS Providers offer this "plain common sense" reading: Assessments for universal service by state commissions constitute regulation of rates or entry for purposes of the statute. The first sentence of this subsection prohibits the states from regulating rates or entry, and therefore prohibits universal service assessments, relating to CMRS providers. The second sentence explains that states may impose universal service requirements "where such services are a substitute for land line telephone exchange service. . . . " This plain language, Celpage and the CMRS Providers argue, expressly prohibits states from requiring universal service contributions from CMRS providers without first making a finding that the CMRS services in question are a substitute for landline telephone service.

The FCC points to plain language that requires it to make "[e]very . . . carrier that provides intrastate telecommunications service" contribute to the universal service programs as determined by the states. *See* 47 U.S.C. § 254(f). It then contends that the provisions of § 332(c)(3)(A) should not be read to trump the express commands of § 254(f).

The FCC finds support for its reading in the second clause of the first sentence of § 332(c)(3)(A). First, it concludes that requiring universal service contributions is neither rate nor entry regulation. *See Fourth Reconsideration Order* ¶ 301. It then notes that this clause says that a state is not prohibited from regulating "other terms and conditions of commercial mobile services." Based on this clause alone, the FCC argues, the states retain the ability to compel universal service contributions as long as it does not constitute regulation of rates or entry. The second sentence simply clarifies that states can also regulate "rates and entry" if they make a finding that CMRS providers are substituting for landline service.

The *Sprint* court adopted this reading of § 332(c)(3)(A) and added another argument for the FCC's position. *See Sprint*, 149 F.3d at 1061. The second sentence's introductory language, "nothing in this subparagraph . . . ," limits the reach of the landline substitution requirement to § 332(c)(3)(A). Therefore, the landline substitution requirement "simply is not relevant to § 254(f)." *Id.*

The petitioners argue that the FCC's reading violates the maxim of statutory construction that all language of a

statute must be given effect.[63] According to the petitioners, if we read the clause "other terms and conditions" to enable states to impose universal service requirements, then the entire second sentence would be redundant. There would be no reason to create a statutory requirement for when states may impose conditions for universal service if the "other terms and conditions" clause already allows states to impose universal service requirements on CMRS providers.

But the FCC persuasively responds that, under its reading, the second sentence clarifies the ability of states to regulate rates and entry in the name of universal service, while the "other terms and conditions" clause opens the door to all other universal service regulation. Thus, we do not conclude, as the petitioners imply we should, that requiring universal service contributions necessarily constitutes the regulation of rates and entry.[64] Thus, under the FCC's reading, the states may generally regulate CMRS providers as they please, but they may regulate the rates and entry of CMRS providers only when they make a finding of substitutability.

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[63] *See Mississippi Poultry Ass'n v. Madigan*, 31 F.3d 293, 304 (5th Cir.1994) (en banc) ("[A] statute should be interpreted so as not to render one part inoperative.").

[64] A state commission could require a universal service contribution based on end-user revenues but leave the carrier free to set its rates as it pleases while not blocking new carriers from entering the market. On the other hand, a state commission would be regulating "rates and entry" if it required the carriers to lower rates for one group of customers as part of an implicit subsidy.

We disagree with the CMRS Providers' further argument that even this reading, adopted in *Cellular Telecomms. Indus. Ass'n v. FCC*, 168 F.3d 1332 (D.C.Cir.1999),[65] would render the second sentence redundant because the third sentence of the subsection specifically lays out the procedures under which a state can petition for the right to regulate CMRS rates. The FCC's reading would still permit the following understanding of the statute: States (1) in general can never regulate rates and entry requirements for CMRS providers; (2) are free to regulate all other terms and conditions of CMRS service; (3) may regulate CMRS rates and entry requirements when they have made a substitutability finding in connection with universal service programs; and (4) may also regulate CMRS rates if they petition the FCC and meet certain statutory requirements, including either substitutability or unjust market rates. None of the provisions would have to be read as inoperative or redundant.

Additionally, this reading would avoid conflict with § 254(f), which requires that "every telecommunications carrier" contribute to the universal service fund. This rendition of § 332(c)(3)(A) allows the FCC to give effect to the plain language of § 254(f) while not violating § 601(c)'s directive to construe the Act in ways that do not "modify, impair, or supersede" federal law.

Therefore, the reading offered by Celpage and the CMRS Providers does not represent the unambiguous intent of Congress. The FCC's reading reflects Congress's

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[65] *See also Sprint Spectrum, L.P. v. State Corp. Comm'n*, 966 F.Supp. 1043 (D.Kan.1997).

unambiguous intent as expressed in the plain language of the statute and takes into account Congress's instruction that § 254 be construed in ways that do not conflict with other federal laws.[66] Therefore, we reject Celpage and the CMRS providers' challenges to this section of the Order.

(b) CMRS Providers as Interstate Carriers.

Celpage and the CMRS Providers raise a weak challenge to state contribution requirements, contending that CMRS providers are "jurisdictionally interstate" and therefore exempt from state assessments. We agree with the FCC that the plain language of § 254(f) simply requires that "[e]very telecommunications carrier that provides intrastate telecommunications services" contribute to state mechanisms. As the agency found, a significant portion of the CMRS providers' services arise from providing *intrastate* telecommunications services.[67] This undeniably significant involvement of CMRS providers in

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[66] Even if the CMRS providers are right that the plain language does not unambiguously support the FCC's reading, we would defer to the FCC's reasonable interpretation under *Chevron* step-two. *Accord Cellular Telecommunications*, 168 F.3d at 1336 ("The bottom line is that Cellular has not demonstrated that its interpretation of § 332(c)(3)(A) is the only permissible one. . . . ").

[67] According to one study, interstate revenues accounted for only 5.6% of total revenues for cellular and personal communications service carriers and 24% of total revenues for paging and other mobile service carriers. *See* Fourth Reconsideration Order ¶ 303.

the provision of intrastate service is more than sufficient to place them within the ambit of § 254(f).

b. Determining That Interstate Carriers Must Contribute on the Basis of Their International Revenues.

COMSAT, a small interstate carrier specializing in providing international telephone service, challenges the FCC's decision to define the universal service base to include the international revenues of interstate carriers. COMSAT derives such a small portion of its revenues from interstate service that it would end up with universal payment obligations exceeding its interstate revenues. It argues that this bizarre outcome violates § 254(d)'s requirement that all universal service contributions be "equitable and nondiscriminatory" and the FCC's own principle of competitive neutrality. At the very least, COMSAT argues, this result shows that the FCC's action is arbitrary and capricious.

As a threshold matter, the FCC challenges the availability of judicial review, because COMSAT failed to petition the agency for reconsideration, as required by § 405 of the Act.[68] COMSAT responds that the absence of a § 405 petition for rehearing is not a bar to judicial review if the petitioner was a party in the rulemaking proceeding and the FCC was afforded an opportunity to rule on the issue.[69] Because COMSAT did participate in the rulemaking

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[68] 47 U.S.C. § 405(a).

[69] "The filing of a petition for reconsideration shall not be a condition precedent to judicial review of any such order,

proceeding and did file comments[70] with the agency on this question, we agree that § 405 does not bar our review.[71]

The FCC is more persuasive when it argues that COMSAT is really asking for consideration of its individual circumstance rather than challenging the rule as a whole. In this situation, the FCC argues that waiver is a more appropriate remedy than is judicial review. In fact, COMSAT did file a petition for waiver but withdrew it without explanation shortly before the FCC filed its brief in this case. COMSAT now claims to be bringing this claim on behalf of all international carriers in similar circumstances, but it fails to identify any such entities and remains alone in its petition for review.

While waiver may be an appropriate remedy, the FCC cites no authority for the proposition that consideration of a waiver is required before judicial review may occur, and our research has found no such authority. The case relied on by the FCC stands only for the proposition

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decision, report, or action, except where the party seeking such review (1) was not a party to the proceedings resulting in such order, decision, report, or action, or (2) relies on questions of fact or law upon which the Commission, or designated authority within the Commission, has been afforded no opportunity to pass." 47 U.S.C. § 405(a).

[70] *See generally Comments of COMSAT Corp.*, CC Docket No. 96-45 (filed Dec. 19, 1996); *Comments of COMSAT Corp.*, CC Docket No. 96-45 (filed April 12, 1996).

[71] *See Time Warner Entertainment Co., L.P. v. FCC*, 144 F.3d 75, 80 (D.C.Cir.1998) ("So long as the issue is necessarily implicated by the argument made to the Commission, section 405 does not bar our review.").

that waiver will be allowed as long as the underlying rule is rational.[72] We see no statutory basis for denying judicial review on the ground that a party must first seek a waiver. Therefore, we consider the rule on its merits.

COMSAT's attack boils down to the argument that it is being unfairly treated because it will be forced to pay more in universal service contributions than it can generate in interstate revenues.[73] It makes a compelling argument that this result alone violates the equitable language of the statute. The FCC's response to the statutory challenge simply states that there is nothing "inequitable" about requiring a carrier benefiting from universal service from contributing to it.

Under this reading, however, it is difficult to know what the FCC would consider inequitable, because any carrier could conceivably benefit from universal service. Obviously, the language also refers to the fairness in the allocation of contribution duties. In this matter, COMSAT can show that it is being forced to pay more under this rule than it can generate in revenues, yet the FCC does not find even this situation "inequitable."

Moreover, the FCC dismisses COMSAT's claim that the agency violates the "nondiscriminatory" requirement of § 254(d) simply by saying that the agency has recognized that some providers of international service will be

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[72] *See National Rural Telecomm. Ass'n v. FCC*, 988 F.2d 174, 181 (D.C.Cir.1993).

[73] COMSAT estimates that the application of the FCC's interpretation would require it to contribute more in universal service fees ($5 million) than it would generate in interstate revenues ($3.8 million).

treated differently from others. But this recognition of discrimination hardly saves the agency from the statutory requirement that contributions are collected on a non-discriminatory basis.

The agency falls back on its discretion, under the statute, to balance the competing concerns set forth in § 254(b), which include the need for sufficient revenues to support universal service. While the statute allows the FCC a considerable amount of discretion, however, that discretion is not absolute. The heavy inequity the rule places on COMSAT and similarly situated carriers cannot simply be dismissed by the agency as a consequence of its administrative discretion.

Therefore, the agency's interpretation of "equitable and nondiscriminatory," allowing it to impose prohibitive costs on carriers such as COMSAT, is "arbitrary and capricious and manifestly contrary to the statute." *Chevron*, 467 U.S. at 844, 104 S.Ct. 2778. COMSAT and carriers like it will contribute more in universal service payments than they will generate from interstate service.[74] Additionally, the FCC's interpretation is "discriminatory," because the agency concedes that its rule damages some international carriers like COMSAT more than it harms others. The agency has offered no reasonable explanation of how this outcome, which will require companies such as COMSAT to incur a loss to participate in interstate

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[74] COMSAT also points out that much of the interstate service it provides is at the request of the government, to ensure service to isolated locations such as Guam and American Samoa.

service, satisfies the statute's "equitable and non-discriminatory" language. We therefore reverse and remand this portion of the Order for further consideration.

6. TIMING.

a. TIMETABLE FOR THE IMPLEMENTATION OF AN EXPLICIT SYSTEM OF UNIVERSAL SERVICE SUPPORT.

On statutory and constitutional grounds, GTE attacks the FCC's timetable for implementation of an explicit system of universal service support.[75] First, GTE argues

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[75] The FCC asks us to bar review of this question, arguing that GTE and SBC are collaterally estopped from litigating it because they did so during challenges to the Access Charge Order in the Eighth Circuit. *See Southwestern Bell*, 153 F.3d at 537. Before applying collateral estoppel, we must first decide whether (1) the issue under consideration is identical to that litigated in the prior action; (2) the issue was fully and vigorously litigated in the prior action; (3) the issue was necessary to support the judgment in the prior case; and (4) there is no special circumstance that would make it unfair to apply the doctrine. *See Winters v. Diamond Shamrock Chem. Co.*, 149 F.3d 387, 391 (5th Cir.1998), *cert. denied*, ___ U.S. ___, 119 S.Ct. 1286, 143 L.Ed.2d 378 (1999).

We agree with the petitioners that the challenge to the FCC's high-cost support timetable is not "identical," for collateral estoppel purposes, to the issue raised in that case. Although the petitioners challenge the coordination between implicit subsidies in the access charge system and those in the new support system, their challenge in this case involves a broader attack on the timing of the entire universal service high-cost support system rather than on just its interactions with the access charge system.

The Eighth Circuit did not consider the contention that GTE brings before us: that the FCC violated § 254(a) by failing to

that the agency's decision to wait until January 1, 2000, before implementing its plan for providing explicit support for universal service violates the statutory requirements of § 254. Second, GTE asserts that the delay in implementation results in an unconstitutional taking.

i. Statutory Language.

GTE contends that the delay in implementation violates § 254(e) because it fails to provide "sufficient" funding to support universal service.[76] In fact, between the Order's release on May 8, 1997, and its implementation on January 1, 2000, the FCC will have provided no explicit support to the ILEC's, while it has already exposed them to outside competition. In theory, then, new entrants could begin "cherry-picking" the ILEC's'

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implement an "explicit" and "sufficient" universal service support system within "fifteen months" of the 1996 Act's enactment. The Eighth Circuit relied on the fact that the deadline for adopting rules on universal service came after the date for adopting rules on opening the market to local competition. *See Southwestern Bell*, 153 F.3d at 537. Therefore, there was no need for that court to decide whether § 254(a) requires full implementation within "fifteen months" of the enactment, and GTE is not collaterally estopped for pursuing its appeal of § 254(a) in this court. *See Winters*, 149 F.3d at 391 n. 3 ("[U]nless prior issue sought to be precluded from relitigation was a 'critical or necessary part' integral to the prior judgment, collateral estoppel may not apply.").

[76] GTE also claims that the FCC's actions violate the "predictable" and "nondiscriminatory" requirements of § 254(b). We see no merit to this contention and focus instead on GTE's best statutory argument, which relies on the use of the term "sufficient" in § 254(e).

best low-cost, high-profit customers, leaving the ILEC's stuck with the high-cost, money-losing customers that are supposed to be supported by the new universal service subsidy system. This would erode the old implicit subsidy system before the FCC had implemented the new explicit subsidy system.

The question is whether the statute's language plainly requires the FCC to have implemented explicit subsidies at the same time that it issued the Order on May 8, 1997. GTE claims the statute requires immediate implementation. But the plain language of § 254(a)(2) requires us to reach the opposite result:

> The Commission shall initiate a single proceeding to implement the recommendations from the Joint Board required by paragraph (1) and shall complete such proceeding within 15 months after February 8, 1996. The rules established by such proceeding shall include a definition of the services that are supported by Federal universal service support mechanisms and *a specific timetable for implementation*.

47 U.S.C. § 254(a)(2) (emphasis added).

By instructing the FCC to establish a "*timetable* for implementation" by the statutory deadline, Congress assumed the implementation process would occur over a transition period after the fifteen-month deadline. There is no reason to believe – and GTE does not offer a reason – that the instruction to establish a timetable actually

means immediate implementation of the explicit subsidy system at the statutory deadline.[77]

Not surprisingly, GTE falls back on the term "sufficient" and argues that even if the FCC may slowly implement the high-cost support program, the statute still requires the agency to ensure that support is sufficient during the transition period. For reasons that we have outlined, the FCC should be accorded a substantial amount of deference when interpreting this word. *See supra* part III.A.a.i.

GTE essentially asks us to hold that "sufficient" is violated whenever there is a change (or the possibility of a change) from the current levels of universal service support. The plain meaning of "sufficient" is far from unambiguous as it pertains to the timing of the high-cost support program's implementation. Calculating how much support is sufficient to provide support for universal service is a judgment the FCC is better able to make than are we, and we therefore defer to its reasonable interpretation under *Chevron* step-two.

As the agency explains, the amount of competition in local markets depends on a number of different factors, of which the implementation of the universal service plan is only one. To enter a new market, entrants must invoke rights to interconnection agreements under §§ 251 and

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[77] Section 254(e) contemplates that universal support will be "explicit" and "sufficient" "[a]fter the date on which Commission regulations implementing this section [§ 254(e)] take effect." This language further supports the FCC's reading that Congress did not require implementation of the high-cost support program immediately after the 15-month deadline.

252.[78] In almost all cases, these agreements require lengthy arbitrations by state commissions. Even after the completion of such arbitrations, there may be many court challenges. Because only competition in local markets can erode the current implicit subsidy system to an insufficient level, the FCC made a reasonable determination that there was little chance of such competition's emerging in the near future.

Where the statutory language does not explicitly command otherwise, we defer to the agency's reasonable judgment about what will constitute "sufficient" support during the transition period from one universal service system to another. We follow the Eighth Circuit's recent holding on a similar issue: "The Commission has made a predictive judgment, based on evidence in the record and adequately explained in the order, that competitive pressures in the local exchange market will not threaten universal service during the interim period until the permanent, explicit universal service support mechanisms have been fully implemented." *Southwestern Bell*, 153 F.3d at 537.

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[78] The Supreme Court did not issue its final word on these sections until January 25, 1999. *See Iowa Utilities*, 119 S.Ct. 721. In the meantime, many potential entrants were stymied in the arbitration process and by the uncertainty over the FCC's jurisdiction to implement its local competition order. Therefore, it is not surprising that the agency did not expect an onslaught of local competition during the interim period.

ii. TAKING.

In some ways, GTE's takings argument is simply another version of its contention regarding lack of "sufficient" support. On both issues, GTE argues that the FCC's decision to leave ILEC's exposed to local competition without first implementing the new universal service plan results in a severe reduction of its revenues from local service. Relying on *Brooks-Scanlon v. Railroad Comm'n*, 251 U.S. 396, 40 S.Ct. 183, 64 L.Ed. 323 (1920), GTE argues that a regulated entity cannot be forced to operate one segment of its business at a loss on the expectation that it can make up the shortfalls from another competitive line of business. At the very least, GTE says, the FCC should adopt a narrow construction of the statutory language to avoid any constitutional infirmities.[79]

The FCC responds that before a narrowing construction should be considered, GTE must show that a taking will "necessarily" result from the regulatory actions. *See United States v. Riverside Bayview Homes*, 474 U.S. 121, 128 n. 5, 106 S.Ct. 455, 88 L.Ed.2d 419 (1985). Even if GTE can show that some taking will result, it must demonstrate that its losses are so significant that the "net effect" is confiscatory. *See Duquesne*, 488 U.S. at 310-16, 109 S.Ct. 609.

GTE has failed to meet the requirements of *Duquesne*, because it cannot show that it will lose any revenue at all,

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[79] *See Edward J. DeBartolo Corp. v. Florida Gulf Coast Building & Constr. Trades Council*, 485 U.S. 568, 575, 108 S.Ct. 1392, 99 L.Ed.2d 645 (1988).

much less enough to constitute a taking under more recent precedent. Its attempt to distinguish *Duquesne* is misguided because, contrary to GTE's claim, the *Duquesne* Court did not base its finding of takings on the fact that the market was no longer closed to competition.

Rather, *Duquesne* stands for the proposition that "no single ratemaking methodology is mandated by the Constitution, which looks to the consequences a governmental authority produces rather than the techniques it employs." *Duquesne*, 488 U.S. at 299, 109 S.Ct. 609 (Scalia, J., concurring). *Duquesne* does not require courts to engage in a takings analysis whenever an agency opens a previously regulated market to competition. Further, as we explained in sustaining the forward-cost looking methodology, GTE's reliance on *Brooks-Scanlon* is misplaced, because we will not apply the rule in that case to transitional or temporary periods. *See Continental Air Lines*, 784 F.2d at 1251.

b. Access Charges at Forward-looking Cost Levels as Soon as Cost Models Are Available.

MCI asks the FCC to reduce access charges – the fees charged by ILEC's on interstate calls – to the forward-looking cost level used by the agency to calculate support for high-cost areas. Under the FCC's plan, ILEC's will be required to reduce their access charges by the amount they receive in the form of explicit universal service subsidies. MCI argues that by permitting the ILEC's to retain the amount of access charge revenue above cost, the FCC has violated its statutory mandate to eliminate

implicit subsidies when it implements the new universal service plan.

This argument differs from GTE's assertions. While GTE seeks immediate implementation of the explicit subsidy program, MCI seeks to include the elimination of implicit subsidies within the rubric of the explicit subsidy program. In fact, GTE's fear that implicit subsidies will be eroded during the transition period is precisely the goal of MCI's intervention. Because GTE does not seek the elimination of the implicit subsidies, it is making an argument different from MCI's.

For this reason, we agree with the FCC that MCI cannot properly intervene on this issue, because none of the petitioners raised the same challenges to the Order. In *United Gas Pipe Line*, 824 F.2d at 437, we held that "intervenors may not challenge aspects of the Commission's orders not raised in the petitions for review." Because MCI's challenge does not raise an issue brought up by any of the petitioners, we do not consider its arguments on appeal, but follow the District of Columbia Circuit and decline to grant intervenor standing in a situation in which "we could grant [the intervenor] the full relief it seeks while rejecting all of the petitioners' challenges, and vice versa." *Illinois Bell Tel. Co. v. FCC*, 911 F.2d 776, 786 (D.C.Cir.1990).[80]

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[80] MCI claims that the FCC is trying to evade review of this question through procedural maneuvering. When BellSouth, in its Eighth Circuit challenge to the Access Charge Order, raised the issue of the FCC's failure to remove all implicit subsidies, the agency argued that this question should be addressed in this court in challenges to the Universal Service Order. Now that

c. Plan for Transition to a New Universal Service System For Rural, Insular, and High-cost Areas..

The FCC's transition plan for its new explicit subsidy universal support system does not immediately apply to all ILEC's. All carriers eligible for universal service support will become part of the new system on January 1, 2000. Small rural carriers, however, will not be required to move into the new system until 2001 at the earliest. *See* Order ¶ 204. Specifically, the agency (1) has exempted rural carriers, defined as those carriers serving study areas of less than 100,000 lines, from the new forward-looking cost methodology until at least January 1, 2001,[81] and (2) has allowed carriers with 200,000 or fewer working loops per study area to continue recovering extra support from the high-cost fund until implementation of the new methodology on January 1, 2000. *See* Order § 210.

MCI has raised that same issue, MCI argues that the agency should not be allowed to dodge review again on procedural grounds.

Unfortunately for MCI, it was not any manipulation of procedural rules by the FCC that prevented MCI from properly raising this issue on appeal. There was no legal reason that prevented MCI from filing a brief as a petitioner rather than as an intervenor. Thus, the FCC's procedural moves are irrelevant for purposes of deciding whether MCI may properly intervene. The only question, then, is whether MCI's challenge to the Order for failing to reduce access charges immediately is the same as GTE's challenge to the Order for failing to implement explicit subsidies immediately. We see no such resemblance.

[81] *See* Order ¶ 273 (stating that "non-rural carriers" will come under the new forward-looking cost methodology).

i. Establishing a Longer Transition Period for Rural Carriers with fewer than 100,000 lines.

Vermont[82] attacks the small rural carrier exemption because it does not permit large carriers who happen to serve rural areas the same delayed transitional treatment that rural carriers with study areas of less than 100,000 lines will receive. Vermont argues that there is no statutory or reasonable basis for distinguishing among rural carriers simply because of their size. For example, census statistics show that Vermont has more residents living in rural areas than does any other state, yet its carrier, Bell Atlantic, does not qualify for the same treatment as do other rural carriers as defined by the FCC's 100,000-line distinctions.

Vermont does not point to any statutory authority for its claim that the FCC must give all rural carriers the same treatment under the plan. Instead, it simply argues there is no good reason to treat Bell Atlantic differently from other rural carriers. For these reasons, it asks us to reverse on arbitrary-and-capricious grounds under the APA.

A statute survives judicial scrutiny under the APA's "arbitrary and capricious" standard as long as the agency "articulates a rational relationship between the facts found and the choice made" and "so long as the agency

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[82] Kansas initially joined Vermont in this challenge but indicates, in its reply brief, that it now withdraws from this portion of the appeal.

gave at least minimal consideration to relevant facts contained in the record." *Harris*, 19 F.3d at 1096. The FCC provides at least two reasons that articulate such a "rational relationship."

First, because the agency delayed the transition for rural carriers on the ground that its cost models for small carriers were inadequate, it was reasonable to treat Bell Atlantic differently. After all, Bell Atlantic is a large ILEC for which the FCC does have cost models. Second, the FCC justifies its delay for small rural carriers because it has found that they will have greater difficulty adjusting to a new system. Again, such a finding would not apply to Bell Atlantic. These reasons suffice.

ii. Continuing Application of Existing High-cost Rules until the New Universal Service system Takes Effect.

Vermont[83] challenges the decision to maintain extra support for ILEC's with study areas of 200,000 or fewer loops until the new methodology is implemented on January 1, 2000. In other words, by exempting carriers with 200,000 or fewer lines from the new high-cost support methodology, the FCC again decided to give extra support to smaller carriers, in this case defined as those carriers with study areas containing 200,000 or fewer loops. As it did in challenging the 100,000 line distinction,

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[83] Kansas initially joined Vermont in this challenge, but has indicated in its reply brief that it now withdraws from this portion of the appeal.

Vermont asserts that the distinction is arbitrary and capricious because the FCC ignores evidence that size is not a reliable predictor of cost.

The FCC again argues that the 200,000-line rule is transitional, interim relief. The agency has stated that the extra support provided by this rule will expire when the new forward-looking cost methodology goes into effect on January 1, 2000. It asks us to accord it the "substantial deference" it needs to develop transitional solutions to complex regulatory problems. *See MCI Telecomms. v. FCC*, 750 F.2d 135, 140 (D.C.Cir.1984).

In contrast to the situation involving the rural carrier exemption, the FCC has set a specific date for the end of this transitional period: January 1, 2000. Accordingly, the agency's commitment to a specific date for termination of the support resulting from the 200,000-loop rule makes the rule sufficiently transitional to avoid judicial review. Therefore, for lack of ripeness, we will not review Vermont's challenge to the effects of the 200,000-loop distinction.[84]

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[84] Vermont argues that the 200,000-loop distinction will become permanent through its incorporation into the "hold harmless" rule articulated in the *Seventh Report and Order*. As we have discussed, *supra*, we do not have jurisdiction to consider the merits of that new Order except in the way that it affects our review of the Order. The "hold harmless" principle was introduced in the *Seventh Report and Order* and remains outside the scope of this proceeding.

B. Subsidization of Services for Schools, Libraries, and Health Care Providers.

Section 254(h) adds a new wrinkle to the concept of universal service by directing the FCC to provide support to elementary and secondary schools, libraries, and health care providers. Thus, the agency has a new statutory mandate to subsidize support for certain beneficiaries, irrespective of whether they are high-cost consumers. GTE raises objections to the agency's implementation of this broad statutory mandate,[85] and Cincinnati Bell and the states challenge the proposal to assess contributions to this new universal service fund.

1. Mandating Support for Internet Access and Internal Connections to Schools and Libraries.

While section 254(h) plainly authorizes the FCC to support discounted telecommunications services to schools and libraries, GTE finds no equivalent statutory authority to support discounted internet access and internal connections. Therefore, GTE argues that the agency

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[85] As a threshold matter, GTE challenges the timing of the proposal, because it would require support for schools, libraries, and health care providers before the new system for explicit subsidies has been implemented. For the same reasons we have discussed, *see supra* part III.A.6.1., we extend the FCC greater discretion in deciding what will be "sufficient" during the transition period, especially when there is little reason to believe that the old subsidy system will break down during that period.

exceeded its statutory authority when it mandated support for discounted internet services and internal connections.

Although we agree with GTE that the statute and its legislative history do not support the FCC's interpretation, the language of the statute is ambiguous enough to require deference under *Chevron* step-two. Because, however, the FCC's decision to extend universal service support to internet access and internal connections raises grave doubts as to whether § 254(h) creates an unconstitutional tax, we construe the statute narrowly to avoid raising these constitutional problems.[86]

The FCC concedes that internet access and internal connections cannot be defined as "telecommunications

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[86] Judge Garza does not join our analysis of the constitutional issues raised by the FCC's decision to provide discounts on internet services for schools and libraries, set forth in note 97, *infra*. He would not address these issues, because the parties did not raise them on appeal. *See Carducci v. Regan*, 714 F.2d 171, 177 (D.C.Cir.1983) (refusing to consider a constitutional issue of first impression "where counsel has made no attempt to address the issue" and "where, as here, important questions of far-reaching significance are involved"). *But see United States Nat'l Bank v. Independent Ins. Agents of Am.*, 508 U.S. 439, 446, 113 S.Ct. 2173, 124 L.Ed.2d 402 (1993) (approving lower court's consideration of legal claim not argued by either party as part of courts' "independent power to identify and apply the proper construction of governing law") (internal quotations omitted); *United States v. Moore*, 110 F.3d 99, 101 (D.C.Cir.1997) (en banc) (Silberman, J., dissenting) (conceding that the "rigor and integrity of *Carducci* was severely impaired by the unanimous decision of the Supreme Court" in *Independent Insurance Agents*).

services" for purposes of the section.[87] It argues, however, that the plain language of § 254(h)(1)(B) and (c)(3) authorizes it to require discounted internet access and internal connections to schools and libraries (but not to health care providers).

Subsection 254(h)(1)(B) requires all telecommunications providers to provide to elementary schools, secondary schools, and libraries, on request, discounted services "that are within the definition of universal service under subsection (c)(3) of this section." Subsection (c)(3) authorizes the FCC to designate "additional services for such support mechanisms for schools, libraries, and health care providers for the purposes of subsection (h) of this section." These "additional services" are "[i]n addition to services included in the definition of universal service under paragraph (1)," which defines universal service as an "evolving level of telecommunications services."

The FCC points out that there is no language restricting these "additional" services to telecommunications services. Furthermore, Congress used the limiting term "telecommunications services" in § 254(h)(1)(A) when discussing the provision of universal service support for rural health care providers. The agency argues that "the varying uses of the terms 'telecommunications services' and 'services' in § 254(h)(1)(A) and (B) suggests that the terms were used consciously to signify different meanings." Order ¶ 439. Therefore, the FCC concluded that the

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[87] The FCC has recognized that internet access or internal connection services are "information services" that cannot be equated with "telecommunications services." *See* Order ¶ 439 n.1145.

term "additional services" is not limited to telecommunications services. It then decided that, based on the legislative history and its understanding of the purposes of the statute, it should require internet access and internal connections[88] support for schools and libraries.

We first consider whether the FCC's interpretation conflicts with the plain language of § 254(h)(1)(B) and (c)(3). Although the best reading of the statute does not authorize the agency's actions, we find the statute sufficiently ambiguous to invoke step-two of *Chevron*.

The statute restricts the FCC's authority to interpret the phrase "additional services" in subsection (c)(3) to "the purposes of subsection (h) of this section." The use of the phrase "telecommunications services" in the title of § 254(h) indicates that the "purposes of subsection (h)" are to provide discounted support for *telecommunications services*.[89]

We find further support for this reading in the legislative history of § 254(h): "New subsection (h) of section

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[88] Calling "internal connections" a good and not a service, GTE separately attacks the "internal connections" requirement. The FCC argues that courts have recognized internal connections as services, *see NARUC v. FCC*, 880 F.2d 422, 430 (D.C.Cir.1989), and that the legislative history's emphasis on connections to "classrooms" makes such a requirement reasonable. Given that the maintenance and installation of regular telephone lines also is characterized as a "service," we reject GTE's attempt to distinguish "internal connections."

[89] *See United States v. Wallington*, 889 F.2d 573, 577 (5th Cir.1989) (stating that the "section heading enacted by Congress in conjunction with statutory text [is considered] to 'come up with the statute's clear and total meaning.' " (citation omitted)).

254 is intended to ensure that health care providers for rural areas, elementary and secondary school classrooms, and libraries have affordable access to modern *telecommunications* services. . . . "[90] The House Conference Report also elaborates on the interaction between subsections (h)(1)(B) and (c)(3):

> New section (h)(1)(B) requires that any telecommunications carrier shall, upon a bona fide request, provide services for educational purposes included in the definition of universal service under new subsection (c)(3) for elementary and secondary schools and libraries at rates that are less than the amounts charged for similar services to other parties, and are necessary to ensure affordable access to and use of such *telecommunications services*.[91]

And while the legislative history of subsection (c)(3) supports giving the FCC discretion when designating services for schools and libraries, it nevertheless describes the subsection (c)(3) definition as "applicable only to public institutional *telecommunications* users."[92] This language provides more evidence that Congress intended that the FCC designate additional *telecommunications* services under subsection (c)(3) rather than any additional services that the agency deems desirable.

Indeed, the agency's broad reading of "additional services" would mean that the use of the word "services"

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[90] H.R. CONF. REP. 104-458, at 132 (1996) (emphasis added), *reprinted in* 1996 U.S.C.C.A.N. at 124, 144.

[91] H.R. CONF. REP. 104-458, at 133 (1996) (emphasis added), *reprinted in* 1996 U.S.C.C.A.N. at 144.

[92] *Id.*

in other parts of § 254(c) could be broadened to include non-telecommunications services. For instance, § 254(c)(2) authorizes the Joint Board to recommend modifications to the definition of "services." Under the FCC's interpretation, the Joint Board (composed of state telecommunications regulators and members of the FCC) could be free to redefine "services" to include services unrelated to telecommunications. This result is an implausible reading of Congress's intent.[93]

This is not the end of the analysis, however, because some aspects of the statute's language and legislative history also support the FCC's reading. First, the plain language of § 254(c)(1) invites the FCC periodically to redefine "universal service" to "tak[e] into account advances in telecommunications and information technologies and services." Moreover, the "purposes of subsection (h)" language in subsection (c)(3) could include more than the "telecommunications services" referred to in § 254(h)'s section heading. After all, subsection (h)(2)(A), which is also one of the "purposes of subsection (h)," instructs the FCC to establish competitively

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[93] We also agree with GTE that the FCC is asserting unlimited authority to prescribe support for whatever it wishes. At oral argument, counsel for the FCC could not point out how its interpretation could be limited even to internet access services. For instance, the agency could not explain why satellite television services or even janitorial services would not fit within its understanding of "additional services." In contrast, the plain language of § 254 provides an easily recognizable limit on FCC authority by confining § 254(h) support to telecommunications services. The superiority of GTE's reading, however, does not necessarily make Congress's intent unambiguous.

neutral rules to "enhance . . . access to advanced telecommunications and information services. . . . "

Finally, some of the legislative history implies that Congress intended for subsection(h) to support internet access:

> [T]he provisions of subsection (h) will help open new worlds of knowledge, learning and education to all Americans – rich and poor, rural and urban. They are intended, for example, to provide the ability to browse library collections, review the collections of museums, or find new information on the treatment of an illness, to Americans everywhere via schools and libraries.[94]

The reference to "brows[ing] library collections" indicates that in drafting subsection (h), Congress envisioned some kind of support for internet access.

The best reading of the relevant statutory language nonetheless indicates that the FCC exceeded its authority by mandating discounts for internet access and internal connections. The statutory invitation in subsection (c)(1) to "re-define" universal service to include information services does not necessarily relate to the FCC's authority under subsection (c)(3).

Additionally, subsection (h)(2)(A) provides the agency only with authority to "establish competitively neutral rules to enhance access" to information services.

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[94] H.R. CONF. REP. 104-458, at 132 (1996), *reprinted in* 1996 U.S.C.C.A.N. at 144.

It does not contain specific language supporting provision of such services "at rates less than the amounts charged for similar services to other parties," as in subsection (h)(1)(B). And finally, the legislative history does not indicate whether Congress thought the statute would enhance access to internet services through discounts on telecommunications services or, instead, through direct subsidies for internet access.

Even though GTE has offered a persuasive reading of the statute, its plain language does not make Congress's intent sufficiently "unambiguous" for *Chevron* step-one review. Therefore, we defer to the FCC's interpretation under *Chevron* step-two and affirm those aspects of the Order providing internet services and internal connections to schools and libraries.[95]

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[95] Before we defer to the FCC's interpretation of an ambiguously worded statute under the deferential *Chevron* step-two standard of review, we consider whether the agency's approach raises constitutional problems that should lead us to construe the statute in the manner urged by GTE. "[W]here a statute is susceptible of two constructions, by one of which grave and doubtful constitutional questions arise and by the other of which such questions are avoided, our duty is to adopt the latter." *Jones v. United States*, 526 U.S. 227, ___, 119 S.Ct. 1215, 1222, 143 L.Ed.2d 311 (1999) (internal citations omitted). This rule "has for so long been applied by this Court that it is beyond debate." *DeBartolo*, 485 U.S. at 574-75, 108 S.Ct. 1392. It is also of such importance that a court will reject an agency interpretation of a statute that would ordinarily receive deference under *Chevron* step-two if it believes the agency's reading raises serious constitutional doubts. *Id.* (construing statute narrowly to avoid First Amendment problem).

We have identified two ways in which the agency's interpretation could raise constitutional concerns that might

2. AUTHORITY TO PROVIDE SUPPORT PAYMENTS TO NON-TELECOMMUNICATIONS ENTITIES THAT PROVIDE INTERNET ACCESS AND INTERNAL CONNECTIONS TO SCHOOLS AND LIBRARIES.

The FCC invokes its rulemaking power under § 254(h)(2)(A) and its "necessary and proper" authority under § 154(i) to provide support payments to non-telecommunications entities that provide internet access and internal connections to schools and libraries. GTE attacks this decision as violating the express intent of Congress as read through the plain language of the statute.

The FCC does not argue that any specific provision of the statute authorizes it to add non-telecommunications companies to the universal service payment system.

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lead us to construe the statute more narrowly. First, the FCC's application of the universal service fund for non-telecommunications services could constitute an improperly delegated tax. Second, its interpretation of the reach of § 254(h)(1)(B) could have transformed the Act into a "bil[l] for raising revenue" in violation of the Origination Clause.

Though it is a close question, we conclude that the FCC's interpretation does not raise sufficiently serious constitutional doubts to override our normal *Chevron* step-two deference. While the relationship between internet services and the public telecommunications network is more attenuated than is that of paging services, *see supra* part III.A.5.a, we are not convinced that even this attenuated relationship raises serious doubts under *Munoz-Flores*. For similar reasons, this attenuated relationship does not raise serious doubts as to whether the FCC's interpretation makes the assessment an improperly delegated tax. *See Rural Tel. Coalition v. FCC*, 838 F.2d 1307, 1314 (D.C.Cir.1988) (rejecting unconstitutional tax challenge to universal service support allocation finding).

Rather, it avers that (1) the statute gives it broad authority to establish competitively neutral rules; (2) the statute does not speak directly to the issue of non-telecommunications providers; and (3) the statute's silence indicates that the agency should receive *Chevron* deference.

GTE relies on the traditional maxim of statutory construction, *"expressio unius est exclusio alterius."*[96] GTE points out that § 254(h)(1)(B) already discusses how carriers will be reimbursed for providing discounted services: "[a] telecommunications carrier providing service under this paragraph. . . . " According to GTE, Congress's choice of the phrase "telecommunications carrier" precludes the FCC from providing those same payments to non-telecommunications carriers.

We conclude that the combination of the FCC's "necessary and proper" authority under § 154(i) and the limited usefulness of the *expressio unius* doctrine in the administrative context permit the FCC to expand the reach of universal support to non-telecommunications carriers. While courts have rightly warned against using silence in a statute to give "agencies virtually limitless hegemony,"[97] we are convinced that Congress intended to allow the FCC broad authority to implement this section of the Act.

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[96] "The expression of one thing implies the exclusion of another." "Hence, a statute that mandates a thing to be done in a given manner . . . normally implies that it shall not be done in any other manner. . . . " 73 AM.JUR.2D *Statutes* § 211 (1995).

[97] *Ethyl Corp. v. EPA*, 51 F.3d 1053, 1060 (D.C.Cir.1995).

In *Iowa Utilities Board v. FCC*, the Eighth Circuit offered this explanation of the reach of § 154(i) in denying the FCC jurisdiction over the pricing of local telephone service: "[Section 154(i)] merely suppl[ies] the FCC with ancillary authority to issue regulations that may be necessary to fulfill its primary directives contained elsewhere in the statute. [It does not] confer [ ] additional substantive authority." 120 F.3d 753, 795 (8th Cir.1997). In this matter, however, the FCC is not asserting additional substantive authority, as it tried to do in *Iowa Utilities*. It is not asserting additional jurisdictional authority, but, rather, is issuing a regulation "necessary to fulfill its primary directives."

The agency's primary directive is to "enhance access to advanced telecommunications and information services" for schools and libraries. *See* § 254(h)(2)(A). It is taking modest steps to ensure that Congress's instructions on expanding universal service in the form of internet access and internal connections will not be frustrated by local monopolies.[98] For these reasons, we affirm the decision to permit support of non-telecommunications carriers providing internet access and internal connections to schools and libraries.

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[98] The District of Columbia Circuit has upheld FCC actions under § 154(i) that require payments from parties even without express statutory authorization. *See Mobile Communications Corp. of Am. v. FCC*, 77 F.3d 1399 (D.C.Cir.1996); *New England Tel. & Tel. Co. v. FCC*, 826 F.2d 1101 (D.C.Cir.1987).

3. Encroaching on State Authority To Set Discount Rates for Intrastate Services to Schools and Libraries.

Section 254(h)(1)(B) divides the regulation of discount rates on services offered to schools and libraries between the FCC and the states. "The discount shall be an amount that the Commission, with respect to interstate services, and the States, with respect to intrastate services, determine is appropriate and necessary to ensure affordable access to and use of such services by such entities." § 254(h)(1)(B).

The FCC has decided to offer federal universal service funds to help support the intrastate rate discounts. Predictably, the agency has conditioned such funding on the states' "establish[ing] intrastate discounts at least equal to the discounts on interstate services." Order ¶ 550. GTE challenges this condition as an encroachment on the states' statutory right to "determine [what is] appropriate and necessary to ensure affordable access."

GTE has failed to point to any statutory or other authority prohibiting the FCC's condition for funding. States are free to refuse federal support for intrastate discounts and, therefore, remain free to determine what is "appropriate and necessary," consistent with the plain language of the statute. In the Tenth Amendment context, this court has refused to view similar federal conditional grants as "equivalent to coercion." *See Texas v. United States*, 106 F.3d 661, 666 (5th Cir.1997). Without express statutory language prohibiting such a practice, we reject GTE's challenge to the FCC's funding conditions.

4. Exercising Authority in Deciding That Schools and Libraries Can Obtain Discounts on All Commercially Available Telecommunications Services.

The FCC has also decided that, pursuant to its authority under § 254(c)(3), it will allow schools and libraries to obtain supported discounts on all commercially available telecommunications services. The agency believes that this approach will maximize schools' and libraries' flexibility to purchase whatever package of services they need.

GTE challenges the agency's statutory authority to refuse to limit the types of services that will be available for support. It contends that the plain language of § 254(c)(3) requires the FCC to "designate" which telecommunications services will receive universal service support and which telecommunications services will not. The key to GTE's argument is the meaning of "designate."

According to GTE, "designate" denotes some action of specific selection. The standard dictionary definition of "designate" includes "to distinguish as to class" and "to indicate and set apart for a specific purpose, office, or duty." Merriam-Webster's Collegiate Dictionary 313 (10th ed.1994). GTE claims that by using the word "designate," Congress instructed the FCC to "indicate and set apart" which services may receive support under § 254(h). GTE also finds support in the legislative history, which says

the FCC should "take into account the *particular* needs of . . . schools and libraries."[99]

We disagree with GTE that the plain-meaning understanding of "designate" demonstrates Congress's unambiguous intent to require the FCC to specify which services will be supported. By using the word "designate," Congress also could have meant for the agency to authorize a broad class of services. Thus, by "designating" all commercially available telecommunications service, the FCC can be said to have "designated" which services may be supported. For this reason, the designation "commercially available telecommunications services" does not violate the plain meaning of the statute under *Chevron* step-one.

Under *Chevron* step-two, the FCC has reasonably concluded that it can fulfill its statutory duty to "designate" while giving schools and libraries the maximum flexibility to choose which services they need. It is not unreasonable for the FCC to conclude that it could best "take into account . . . the particular needs" of schools and libraries by allowing support for all commercially available telecommunications services.[100] Because Congress's use of "designate" in subsection (c)(3) does not unambiguously require the FCC to limit which services may be supported, and because the FCC's decision is reasonable

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[99] *See* H.R. CONF. REP. 104-458, at 133 (emphasis added), *reprinted at* 1996 U.S.C.C.A.N. at 144.

[100] The FCC further concluded that its decision will ensure that schools and libraries can obtain discounted "state-of-the-art telecommunications technologies as those technologies become available." *Order* ¶ 433.

under *Chevron* step-two, we reject GTE's request and affirm the decision to allow schools and libraries to obtain support for all "commercially available telecommunications services."

5. Authority To Subsidize Toll-Free Telephone Calls to Internet Service Providers by Non-rural Health Care Providers.

Congress directed the FCC to provide universal service support for "any public or nonprofit health provider that serves persons who reside in rural areas." § 254(h)(1)(A). Congress also instructed the agency "to enhance, to the extent technically feasible and economically reasonable, access to advanced telecommunications and information services for all public and nonprofit . . . health care providers." The FCC has seized on the more general language in the second provision as authority for subsidizing telephone calls to internet service providers by both rural and non-rural health care providers.

GTE advances an argument based on the *expressio unius* canon. Because the first provision gives specific instructions on providing subsidized support for health care providers and explicitly limits that support to rural health care providers, GTE argues that the FCC has no statutory authority to expand such support to non-rural health care providers. In GTE's view, Congress could have extended support to non-rural providers, but chose not to. This signifies a Congressional decision that the FCC should respect.

The FCC responds that the *expressio unius* canon should not resolve a question of statutory interpretation

in an administrative law context. Additionally, it argues that § 254(h)(2)(A) *obligates* the FCC to "enhance, to the extent technically feasible and economically reasonable, access to advanced telecommunications and information services."

We do not read § 254(h)(2)(A)'s "enhancing" language to *require* the FCC to act as it did here. But, we conclude that the language in § 254(h)(2)(A) demonstrates Congress's intent to authorize expanding support to "advanced services," when possible, for non-rural health providers.

GTE has already established that § 254(h)(1)(A) requires support for telecommunications service to rural health care providers only. We can then read § 254(h)(2)(A) as an instruction to the FCC to work to support "advanced services" for non-rural health care providers when "economically reasonable." Importantly, the FCC's plan does not extend, to non-rural health providers, the same telecommunications discounts enjoyed by § 254(h)(1)(A) rural health providers. Rather, the agency chose to support *access* (through subsidized telephone calls) to an "advanced . . . information service" (an internet service provider), finding that this subsidy was "economically reasonable" and "technically feasible." Order ¶ 748.

The FCC has found a way to "enhance access," as authorized by the plain language of § 254(h)(2)(A), so we affirm this portion of the Order.

6. Contribution System To Provide Universal Service Funding for Schools, Libraries, and Rural Health Providers.

The FCC decided to fund the universal support mechanisms for schools, libraries, and rural health care providers by "assessing both the interstate and intrastate revenues of providers of interstate telecommunications services." Order ¶ 808. The uncertainty of state support for the new § 254(h) subsidies and other financial considerations, according to the FCC, justifies assessing both the intrastate and interstate revenues of interstate carriers.

Cincinnati Bell ("CBT"), a small carrier with a mostly intrastate revenue base, attacks the decision as a violation of § 2(b)'s prohibition on federal regulation of intrastate services. The states challenge the FCC's related assertion that it has the authority to require carriers to recover their intrastate contributions from the states.

a. Authority To Assess Contributions on the Combined Interstate and Intrastate Revenues of Carriers That Provide Interstate Telecommunications Services.

Along the same lines as Bell Atlantic's challenge to the "no disconnect" rule, CBT argues that the FCC's decision to assess intrastate revenues exceeds its jurisdiction, in violation of the still-intact *Louisiana PSC* reading of § 2(b). CBT contends that unlike the provisions considered in *Iowa Utilities*, § 254 does not "apply" to intrastate matters in a sufficiently unambiguously manner so as to confer federal jurisdiction.

As we have discussed, we understand § 2(b) to serve as both a rule of statutory construction in considering whether a provision applies to intrastate matters and as a jurisdictional fence against assertions of the FCC's ancillary jurisdiction. *See Iowa Utilities*, 119 S.Ct. at 731. Like *Bell Atlantic*, CBT is using § 2(b) to challenge the FCC's construction of § 254 to *apply* to intrastate ratemaking.

The FCC's first defense denies that its actions even constitute a "regulation" that would fall under the rule of statutory construction created by § 2(b) and *Louisiana PSC*. The agency argues that simply factoring intrastate revenues into calculations of universal service contributions does not constitute regulation of those services. The FCC has used both intrastate and interstate revenues as a basis for imposing accounting obligations or tariff requirements in other contexts without any court's finding § 2(b) violations. Additionally, the FCC has stated that carriers may recover their contributions only from *interstate* rates. The agency believes this last requirement will prevent its contribution requirements from improperly affecting intrastate rates.

Despite the persuasiveness of this argument, we conclude that § 2(b)'s broad language encompasses the FCC's decision to assess intrastate revenues. The plain language of § 2(b) discusses "jurisdiction with respect to . . . charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service. . . . " We agree with CBT that the inclusion of intrastate revenues in the calculation of universal service contributions easily constitutes a "charge . . . in connection with intrastate communication service."

The plain language of § 2(b) directs courts to consider FCC jurisdiction over a very broad swathe of intrastate services. We decline to exempt the FCC's assessment of intrastate revenues from the ambit of § 2(b).[101]

The FCC then contends that § 254 does apply to intrastate matters, because it unambiguously authorizes the agency to develop universal service mechanisms that are sufficient to support both interstate and intrastate service. In support of this assertion, the agency points to § 254(d)'s requirement that "[e]very telecommunications carrier that provides interstate telecommunications services shall contribute . . . to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service." The FCC then compares this language to § 254(f), which allows states to adopt universal service regulations as long as they do not "rely on or burden Federal universal service support mechanisms." This language, the FCC claims, shows that

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[101] The FCC's decision to prohibit carriers from recovering through intrastate rates does not save it from § 2(b) analysis. There is no question that the amount of a carrier's universal service contributions will increase with the inclusion of intrastate revenues. This cost, even if recovered only through interstate revenues, still constitutes a "charge in connection with intrastate service" under § 2(b).

If the point of § 2(b) was to protect state authority over intrastate service, allowing the FCC to assess contributions based on intrastate revenues could certainly affect carriers' business decisions on how much intrastate service to provide or what kind it can afford to provide. This federal influence over intrastate services is precisely the type of intervention that § 2(b) is designed to prevent.

Congress intended for it to bear the primary responsibility for ensuring the sufficiency of universal service for both interstate and intrastate services.

These two provisions do not reflect enough of an unambiguous grant of authority to overcome the presumption established by § 2(b). While, under *Chevron* step-two, we usually give the agency deference in its interpretation of ambiguous statutory language, the Supreme Court continues to require the agency to overcome the § 2(b) statutory presumption with unambiguous language showing that the statute applies to intrastate matters. *See Iowa Utilities*, 119 S.Ct. at 731.

While the text of the statute does not impose any limitation on how universal service will be funded, it also does not explicitly state that the FCC has the responsibility to fund intrastate universal services. The agency seeks authority "in the broad language" of the statute, but "we do not find the meaning of the section so unambiguous or straightforward as to override the command of § 152(b)." *See Iowa Utilities*, 119 S.Ct. at 731 (quoting *Louisiana PSC*, 476 U.S. at 377, 106 S.Ct. 1890).

Without a finding that § 254 applies, the FCC has no other basis to assert jurisdiction, because *Iowa Utilities* explicitly prohibits FCC jurisdiction over intrastate matters stemming from the agency's plenary powers. *See id.* Therefore, we reverse that portion of the Order that includes intrastate revenues in the calculation of universal service contributions.

b. Authority To Refer Carriers to the States To Seek Recovery of Intrastate Contributions.

Though it stated that it had "the authority to refer carriers to the states to seek authority to recover a portion of their intrastate contribution from intrastate rates," Order ¶ 818, the FCC also declined to exercise this authority. Instead, it directed carriers to recover their contributions from interstate revenues only.

The states and CBT challenge this assertion of authority on the same grounds they question the inclusion of intrastate revenues for universal service contributions. Because the FCC bases its authority on the same provisions it cited on that issue, our decision to deny the agency jurisdiction on that question applies equally to the its claim of authority to assess intrastate rates.

The FCC also raises a prudential defense, arguing that because it has not chosen to exercise its authority, the issue is not yet ripe for judicial review. Additionally, the agency argues that both petitioners lack standing. We do not accept either of these prudential defenses.

i. Ripeness.

Conceding that the FCC has not yet acted on its decision to assert authority over intrastate services, the states reject the agency's ripeness claim because the "question presented is purely legal." *See New Orleans Pub. Serv., Inc. v. Council of the City of New Orleans*, 833 F.2d

583, 587 (5th Cir.1987).[102] Pointing also to *Pacific Gas & Elec. Co. v. State Energy Resources Conservation & Dev. Comm'n*, 461 U.S. 190, 103 S.Ct. 1713, 75 L.Ed.2d 752 (1983), the states argue that when the FCC has asserted its authority in a final decision on a legal question such as its jurisdiction over intrastate rates, "one does not have to await the ultimate impact of the threatened injury to obtain preventive relief." *See id.* at 201, 103 S.Ct. 1713.

This issue is ripe for judicial review. The two factors for considering ripeness – fitness for judicial decision and hardship to the parties – support our consideration of this question. Courts should be able to resolve a question such as jurisdiction and authority under the Act. Additionally, the states already have shown one example of the harm in withholding review. For instance, MCI, in the face of state opposition, has already begun billing some customers based on revenue from intrastate calls.[103]

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[102] In its most recent action, the FCC reaffirmed its jurisdictional authority to require carriers to contribute based on both intrastate and interstate revenues. *See Seventh Report and Order* ¶¶ 87-90. In fact, the FCC appears to be awaiting a decision by this court before taking further action: "Accordingly, pending further resolution of this matter by the Fifth Circuit, the assessment base and recovery base for contributions to the high-cost and low-income universal service support mechanism that we adopted in the *First Report and Order* shall remain in effect." *Seventh Report and Order* ¶ 90. This invitation to judicial action further undercuts the FCC's ripeness defense.

[103] MCI has filed a supplemental brief rejecting this characterization. It relies on *MCI Telecomm. Corp. v. Virginia State Corp. Com'n*, 11 F.Supp.2d 669 (E.D.Va.1998), *vacated as moot*, 1999 WL 302325 (4th Cir.1999) (unpublished), in which the court granted MCI's motion for injunctive relief from a Virginia state

ii. STANDING.

The FCC's standing defense has even less merit. First, states have a sovereign interest in "the power to create and enforce a legal code." *See Alfred L. Snapp & Son, Inc. v. Puerto Rico*, 458 U.S. 592, 601, 102 S.Ct. 3260, 73 L.Ed.2d 995 (1982). Moreover, the FCC's refusal to exercise its declared authority does not deprive states of standing. The states point out that the District of Columbia Circuit will not find a lack of standing simply because an agency has refused to enforce its own regulations. *See Alaska v. United States Dep't of Transp.*, 868 F.2d 441, 444 (D.C.Cir.1989). For the same reasons, we also reject the FCC's standing defense.

iii. MERITS.

Having disposed of the FCC's prudential defenses, we reverse its claim that it can refer these carriers to the states for recovery of those contributions. This is for the same reasons that we reject the agency's assertions of jurisdiction to assess intrastate revenues for contributions. The FCC has failed to point to any statutory authority that explicitly demonstrates how § 254 applies to

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commission's order and ruling that MCI's disputed charges were not charges for intrastate calls. MCI also points to the FCC's recent order rejecting Virginia's administrative petition of the same issue. *See Virginia State Corp. Com'n v. MCI Telecomm. Corp.*, No. E-99-01.FCC 99-42 (released Mar. 22, 1999). This ruling actually supports the states' ripeness argument, however, because the district court's final order on this question, along with the FCC's recent order, further demonstrates the propriety of judicial review of this question.

intrastate universal service. Therefore, we deny the agency's claim of jurisdiction and reverse this portion of the Order.[104]

IV. Conclusion.

It is difficult to disagree with the Supreme Court's assessment that the Act is "a model of ambiguity or indeed even self-contradiction." *Iowa Utilities*, 119 S.Ct. at 738. As the Court notes, Congress realizes that many of these ambiguities will be resolved by the FCC during its implementation of the statute, and we, like the Court, generally defer to the agency's interpretation of the sometimes-mysterious sections. *See Chevron*, 467 U.S. at 842-43, 104 S.Ct. 2778. In this case, we have done so, and we affirm most aspects of the Order implementing the universal service program and dismiss challenges to several parts of the Order as moot.

Still, our deferential approach does not require us to affirm the FCC in every circumstance. In particular, the agency exceeded its statutory authority in (1) prohibiting the states from imposing eligibility requirements and (2) requiring ILEC's to recover their contributions from access charges. Applying the Court's most recent pronouncements on the Act, we also deny the FCC jurisdiction over state control of local service disconnections and

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[104] Having concluded that the FCC has no jurisdiction over intrastate rates for universal service purposes, we do not reach CBT's final argument challenging the agency's requirement that carriers recover their contributions solely from interstate revenues.

universal service contributions based on intrastate revenues. We remand one petition to the agency for reconsideration, so it can reconsider the propriety of assessing the international revenues of interstate carriers.

For the reasons stated, the petitions for review are GRANTED IN PART and DENIED IN PART. The May 8, 1997, Universal Service Order is AFFIRMED in part, REMANDED in part, and REVERSED in part, in accordance with this opinion.

APPENDIX B

IN THE UNITED STATES COURT OF APPEALS

FOR THE FIFTH CIRCUIT

No. 97-60421

TEXAS OFFICE OF PUBLIC UTILITY COUNSEL; CELPAGE, INC.; SOUTHWESTERN BELL TELEPHONE COMPANY; GTE MIDWEST, INC.; LOUISIANA PUBLIC SERVICE COMMISSION; COMSAT CORPORATION; PEOPLE OF THE STATE OF CALIFORNIA; PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA; IOWA UTILITIES BOARD; SOUTH DAKOTA PUBLIC UTILITIES COMMISSION; PENNSYLVANIA PUBLIC UTILITY COMMISSION; BELL ATLANTIC TELEPHONE COMPANIES; VERMONT DEPARTMENT OF PUBLIC SERVICE; GTE SERVICE CORPORATION; GTE ALASKA INCORPORATED; GTE ARKANSAS INCORPORATED; GTE CALIFORNIA INCORPORATED; GTE FLORIDA INCORPORATED; GTE SOUTH INCORPORATED; GTE SOUTHWEST INCORPORATED; GTE NORTH INCORPORATED; GTE NORTHWEST INCORPORATED; GTE HAWAIIAN TELEPHONE COMPANY INCORPORATED; GTE WEST COAST INCORPORATED; CONTEL OF CALIFORNIA, INC.; CONTEL OF MINNESOTA, INC.; CONTEL OF THE SOUTH, INC.; PUBLIC SERVICE COMMISSION OF NEVADA; CINCINNATI BELL TELEPHONE COMPANY; FLORIDA PUBLIC SERVICE COMMISSION; PEOPLE OF THE STATE OF NEW YORK;

and

THE STATE CORPORATION COMMISSION OF THE STATE OF KANSAS,

Petitioners,

versus

FEDERAL COMMUNICATIONS COMMISSION

and

UNITED STATES OF AMERICA,

Respondents.

Petitions for Review of an Order
of the Federal Communications Commission

ON PETITIONS FOR REHEARING AND
PETITIONS FOR REHEARING EN BANC

(Opinion 183 F.3d 393 (5th Cir. July 30, 1999)

(Filed Sept. 28, 1999)

Before SMITH, DUHÉ, and EMILIO M. GARZA,
Circuit Judges.

PER CURIAM:

The petitions for rehearing are DENIED, and no member of this panel or judge in regular active service having requested that the court be polled on rehearing en

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* Chief Judge King and Judges Jolly, Higginbotham, Jones, and Barksdale did not participate in the consideration of the petitions for rehearing or the petitions for rehearing en banc.

banc (FED. R. APP. P. 35 and 5TH CIR. R. 35), the petitions for rehearing en banc are DENIED.

ENTERED FOR THE COURT:

/s/ Jerry E. Smith
United States Circuit Judge

APPENDIX C

Federal Communications Commission FCC 97-157

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45

REPORT AND ORDER

Adopted: May 7, 1997 Released: May 8, 1997

By the Commission (Chairman Hundt and Commissioners Quello and Ness concurring and issuing separate statements; Commissioner Chong concurring in part and dissenting in part and issuing a separate statement):

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Appendix M (Future Proceedings)

I. INTRODUCTION

1. In the Telecommunications Act of 1996 (1996 Act),[1] Congress directed the Commission and states to take the steps necessary to establish support mechanisms to ensure the delivery of affordable telecommunications

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[1] Pub. L. No. 104-104, 110 Stat. 56. The 1996 Act amends the Communications Act of 1934, 47 U.S.C. §§ 151 *et seq.* (Act). Hereinafter, all citations to the Act and to the 1996 Act will be to the relevant section of the United States Code unless otherwise noted.

service to all Americans, including low-income consumers, eligible schools and libraries, and rural health care providers. Specifically, Congress directed the Commission and the states to devise methods to ensure that "[c]onsumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas . . . have access to telecommunications and information services . . . at rates that are reasonably comparable to rates charged for similar services in urban areas."[2] Congress further directed the Commission to define additional services for support for eligible schools, libraries, and health care providers, and directed the Commission to "establish competitively neutral rules . . . to enhance, to the extent technically feasible and economically reasonable, access to advanced telecommunications and information services for all public and non-profit elementary and secondary school classrooms, health care providers, and libraries."[3]

2. This Order sets forth a plan that satisfies all of the statutory requirements, and puts in place a universal service support system that will be sustainable in an

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[2] 47 U.S.C. § 254(b)(3).

[3] 47 U.S.C. § 254(h)(2)(A). Telecommunications carriers are required to provide service to rural health care providers "at rates that are reasonably comparable to rates charged for similar services in urban areas." 47 U.S.C. § 254(h)(1)(A). Schools and libraries now are entitled under federal law to service "at rates less than the amounts charged for similar services to other parties." 47 U.S.C. § 254(h)(1)(b). In addition, Congress directed the Commission to "enhance . . . access to advanced telecommunications and information services for all public and non-profit elementary and secondary school classrooms, health care providers, and libraries." 47 U.S.C. § 254(h)(2).

increasingly competitive marketplace. Consistent with the explicit statutory principles, our immediate implementation of section 254 is shaped by our commitment to achieve four critical goals. First, we must implement all of the universal service objectives established by the Act, including those for low-income individuals, consumers in rural, insular, and high cost areas, schools, libraries, and rural health care providers.[4] Second, we must maintain rates for basic residential service at affordable levels. We believe that the rates for this service are generally at affordable levels today. Third, we must ensure affordable basic service continues to be available to all users through an explicit universal service funding mechanism. For the present, we believe we can achieve this goal by maintaining our existing high cost mechanism at current funding levels, picking a platform mechanism by December 1997, and implementing a forward-looking economic cost mechanism for universal service for non-rural carriers starting January 1, 1999. Fourth, we must bring the benefits of competition to as many consumers as possible. To implement this goal, we must, in our access charge reform proceeding, address the implicit subsidies in interstate access charges.

3. Today, we adopt rules that reflect virtually all of the Joint Board's recommendations[5] and fulfill the universal service goals established by Congress. We recognize, however, that future developments in the competitive telecommunications marketplace and the

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[4] *See, e.g.*, 47 U.S.C. §§ 254(b), (h), and (i).

[5] *See* Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Recommended Decision*, 12 FCC Rcd 87 (1996).

necessary actions of the states may warrant further Commission action to ensure that we create sustainable and harmonious federal and state methods of continuously fulfilling universal service goals. Therefore, we will seek additional fact-finding and deliberation by the Joint Board, and further coordination with individual state commissions, during approximately the next fifteen months. With the benefit of further specific recommendations from the Joint Board, specifically on the implementation of support for rural, insular, and high cost areas, this Commission will act not later than August 1998. By adopting in large measure the recommendations of the Federal-State Joint Board and referring several issues to the Joint Board for further review, we commit ourselves to working in close partnership with the states to create complimentary federal and state universal service support mechanisms.

4. This proceeding is part of a trilogy of actions that are focused on achieving Congress's goal of establishing a "pro-competitive, de-regulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans by opening up all telecommunications markets to competition."[6] The other components of the trilogy are the local

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[6] Joint Explanatory Statement at 1.

competition[7] and access reform rulemakings.[8]

Pursuant to the mandate of the 1996 Act, these three proceedings are collectively intended to encourage the development of competition in all telecommunications markets.

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[7] Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, CC Docket No. 96-98, *First Report and Order*, 11 FCC Rcd 15499 (1996) (*Local Competition Order*) *stayed in part pending judicial review sub nom. Iowa Utils. Bd. v. FCC*, 109 F.3rd 418 (8th Cir. 1996). *See also* Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, Area Code Relief Plan for Dallas and Houston Ordered by the Public Utilities Commission of Texas, and Administration of the North American Numbering Plan, Second Report and Order, and Memorandum Opinion and Order, 11 FCC Rcd 19392 (*Local Competition Second Report and Order*).

[8] Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing and End User Common Line Charges, CC Docket Nos. 96-262, 94-1, 91-213, and 95-72, *Notice of Proposed Rulemaking,Third Report and Other and Notice of Inquiry*, 62 Fed.Reg. 4,670 (rel. Dec. 24, 1996) (*Access Reform NPRM*); *First Report and Order*, FCC 97-158 (adopted May 7, 1997) (*Access Charge Reform Order*). *See also* Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, *Fourth Report and Order*, FCC 97-159 (adopted May 7, 1997).

5. In the *Local Competition Order*,[9] we set forth rules to implement sections 251 and 252 of the Communications Act. As with all of Part II of Title II of the Communications Act, those sections, and the rules implementing them, seek to remove the legal, regulatory, economic, and operational barriers to local telecommunications competition. Sections 251 and 252 provide entrants with the opportunity to compete for consumers in local markets by either constructing new facilities, purchasing access to unbundled network elements, or reselling telecommunication services.

6. Through this Order and our accompanying *Access Charge Reform Order*, we establish the definition of services to be supported by federal universal service support mechanisms and the specific timetable for implementation. We set in place rules that will identify and convert existing federal universal service support in the interstate high cost fund, the dial equipment minutes (DEM) weighting program, Long Term Support (LTS), Lifeline, Link Up, and interstate access charges to explicit competitively neutral federal universal service support mechanisms. We will provide universal service support to carriers serving rural, insular, and high cost areas through a mechanism based on forward-looking economic cost beginning on January 1, 1999, for areas served by non-rural LECs, and establish the process to determine

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[9] The pricing provisions and the "pick and choose" rule in the *Local Competition Order* have been stayed. On November 1, 1996, the court reinstated the Commission's "reciprocal compensation" requirements, which dictate how local exchange carriers (LECs) and wireless carriers are compensated for transporting and terminating each other's traffic. *See supra* note 7.

a forward-looking economic cost methodology for areas served by rural LECs. That mechanism will – based upon cost studies states will conduct during the coming year or, at the state's election, based upon Commission-developed methods – calculate the forward-looking economic cost of providing service to consumers in a particular rural, insular, or high cost area. In this proceeding, we modify the funding methods for the existing federal universal service support mechanisms so that such support is not generated, as at present, entirely through charges imposed on long distance carriers. Instead, as the statute requires, we will require equitable and non-discriminatory contributions from all providers of interstate telecommunications service. We also take other steps to make federal universal service support mechanisms consistent with the development of local service competition.

7. When it enacted section 254 of the Communications Act, Congress set forth the principles to guide universal service reform. It placed on the Commission the duty to implement these principles in a manner consistent with the pro-competition purposes of the Act. It also emphasized that the preservation and advancement of universal service was to be the result of federal and state action, stating "[t]here should be specific, predictable and sufficient Federal *and State* mechanisms to preserve and advance universal service."[10] Congress also entrusted the states with a role in universal service, including expressly granting states the authority "to adopt regulations not inconsistent with the Commission's rules to preserve and

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[10] 47 U.S.C. § 254(b)(5) (emphasis added).

advance universal service," and requiring every telecommunications carrier that provides intrastate telecommunications services to "contribute, on an equitable and nondiscriminatory basis, in a manner determined by the state, to the preservation and advancement of universal service in that state" when such state establishes universal service support mechanisms.[11] States traditionally have promoted universal service by, among other things, assuring affordable residential access by explicitly and implicitly subsidizing and pricing basic telephone service at levels associated with very high telephone subscribership rates, currently 94.2%.[12]

8. Universal service support mechanisms that are designed to increase subscribership by keeping rates affordable will benefit everyone in the country, including those who can afford basic telephone service. At the simplest level, increasing the number of people connected to the telecommunications network makes the network more valuable to all of its users by increasing its usefulness to them. Increasing subscribership also benefits society in ways unrelated to the value of the network per se. For example, all of us benefit from the widespread availability of basic public safety services, such as 911.

9. Congress also specified that universal service support "should be explicit," and that, with respect to federal universal service support, "every telecommunications carrier that provides interstate telecommunications

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[11] 47 U.S.C. § 254(f).

[12] States also have done much to enhance access in schools and other specific targeted areas, and for low-income consumers and other specific targeted groups.

services shall contribute, on an equitable and non-discriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service."[13] As explained further in the Joint Explanatory Statement of the Committee of the Conference, Congress intended that, to the extent possible, "any support mechanisms continued or created under new section 254 should be explicit, rather than implicit as many support mechanisms are today."[14]

10. Today, universal service is achieved largely through implicit subsidies.[15] The Commission currently has in place some explicit support mechanisms directed at increasing network subscribership by reducing rates in high cost areas (the high cost fund and Long Term Support) and at making service affordable for low-income consumers (the Lifeline and Link Up programs). The current "system," however, consists principally of a number of implicit mechanisms at the state and, to a substantially lesser extent, federal levels designed to shift

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[13] 47 U.S.C. § 254(d)-(e).

[14] Joint Explanatory Statement of the Committee of the Conference (H.R. Rep. No. 458, 104th Cong., 2d Sess.) (Joint Explanatory Statement) at 131.

[15] When we refer to "implicit subsidies" in this discussion we generally mean that a single company is expected to obtain revenues from sources at levels above "cost" (i.e., above competitive price levels), and to price other services allegedly below cost. Such intra-company subsidies are typically regulated by states. An example at the federal level, however, is the geographic averaging of interstate long distance rates. In section 254(g) of the Act, Congress expressly directed that this implicit subsidy continue.

costs from rural to urban areas, from residential to business customers, and from local to long distance service.

11. The urban-to-rural subsidy has been accomplished through the explicit high cost fund mentioned above, and through geographic rate averaging. The result of state requirements that local telephone rates be averaged across the state is that high-density (urban) areas, where costs are typically lower, subsidize low-density (rural) areas. State pricing rules have also in many cases created a business-to-residential subsidy. Most states have established local rate levels such that businesses pay more on a per-line basis for basic local service than do residential customers,[16] although the costs of providing business and residential lines are generally the same.[17] In addition, rates charged for vertical services such as touch tone, conference calling and speed dialing, subsidize basic local service rates. Finally, interstate and intrastate access charges are set relatively high in order to cover certain loop costs not recovered through local rates. These usage-based charges are then recovered through higher usage charges for interstate long distance service. Thus, interstate long distance customers – and particularly those with higher calling volumes – indirectly subsidize local telephone rates.

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[16] Federal Communications Commission, Common Carrier Bureau, Industry Analysis Division, *Reference Book of Rates, Price Indices, and Household Expenditures for Telephone Service*, tbls. 2-3 (Mar. 1997).

[17] To the extent businesses tend to be concentrated in areas with relatively dense populations, business loops are shorter and, therefore, less costly to serve.

12. Of the three implicit subsidy mechanisms – geographic rate averaging, subsidizing residential lines via business lines, and interstate access charges – only the interstate access charge system has been regulated by the Commission, and this contributes the smallest subsidy of the three. Thus, a number of factors operate today to keep basic local telephone rates low, and Congress ordered that we devise a coordinated federal-state scheme to achieve universal service goals.

13. By our Orders today, we reject the arguments made by some parties that section 254 compels us immediately to remove all universal service costs from interstate access charges.[18] As stated previously, we have met section 254's clear command that we identify the services to be supported by federal universal service support mechanisms, and that we establish a specific timetable for implementation. Under that timetable, we will over the next year identify implicit interstate universal support and make that support explicit, as further provided by section 254(e). Moreover, as with any implicit support mechanism, universal service costs are presently intermingled with all other costs, including the forward-looking economic cost of interstate access and historic costs associated with the provision of interstate access services. We cannot remove universal service costs from interstate access charges until we can identify those costs, which we will not be able to do even for non-rural incumbent local exchange carriers (ILECs) before January 1, 1999.

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[18] *See, e.g., Access Charge Reform Order* at section IV.A.

14. We do not, by our Order today, attempt to identify existing implicit universal service support presently effected through intrastate rates or other state mechanisms, nor do we attempt to convert such implicit intrastate support into explicit federal universal service support. The Commission, in light of section 2(b) of the Communications Act,[19] does not have control over the local rate-setting process, which generally has aimed at ensuring affordable residential rates. States have maintained low residential basic service rates through, among other things, a combination of: geographic rate averaging, higher rates for business customers, higher intrastate access rates, higher rates for intrastate toll service, and higher rates for vertical features. States, acting pursuant to sections 254(f) and 253 of the Communications Act, must in the first instance be responsible for identifying intrastate implicit universal service support. We further believe that, as competition develops, the marketplace itself will identify intrastate implicit universal service support, and that states will be compelled by those marketplace forces to move that support to explicit, sustainable mechanisms consistent with section 254(f). As states do so, we will be able to assess whether additional federal universal service support is necessary to ensure that

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[19] Section 2(b) of the Act provides that in most cases, "nothing in this Act shall be construed to apply or to give the Commission jurisdiction with respect to . . . charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier." 47 U.S.C. § 152(b).

quality services remain "available at just, reasonable and affordable rates."[20]

15. Federal universal service support will be distributed based on the interstate portion of the difference between the forward-looking economic cost of providing service and a nationwide revenue benchmark. The amount of support will be explicitly calculable and identifiable by competing carriers, and will be portable among competing carriers, i.e., distributed to the eligible telecommunications carrier chosen by the customer. It will be funded by equitable and non-discriminatory contributions from all carriers that provide interstate telecommunications services. In the *Access Charge Reform Order* that we also adopt today, we direct that federal universal service support received by ILECs be used to satisfy the interstate revenue requirement otherwise collected through interstate access charges. Accordingly, through this Order and the *Access Charge Reform Order*, interstate implicit support for universal service will be identified and removed from interstate access charges, and will be provided through explicit interstate universal service support mechanisms. To the extent that we fail to identify a source of implicit support, we are confident that the marketplace will, as competition develops, highlight it for further Commission attention.

16. We wish to avoid action that directly or indirectly raises the price of the basic residential telephone

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[20] 47 U.S.C. § 254(b)(1).

service that guarantees access to the local telephone network. We also believe, as did the Joint Board,[21] that raising the existing flat-rate charge on every consumer's line for access to interstate telephone service – the subscriber line charge (SLC) on primary residential lines – is not desirable, because it could adversely affect the affordability of local service. Therefore, we decide in today's Order and its companion *Access Charge Reform Order* that we will not permit any increase in the primary residential line SLC and will not order the creation of any additional end-user charges for local service over these lines. Our primary reason for not mandating the recovery of universal service contributions through basic rates, directly raising charges for basic access through an increase in the primary residence SLC, or adopting any new end-user charge from the local telephone company to the residential consumer for basic access is that we have high subscribership rates today, and therefore believe that current rate levels are "affordable." We see no reason to jeopardize affordability by raising rate levels.

17. At present, the existing system of largely implicit subsidies can continue to serve its purpose, and our current implementation of section 254 relies principally on the continuation of existing mechanisms, with modifications to make them more consistent with the statutory requirements and principles. This system is not sustainable in its current form in a competitive environment. Implicit subsidies were sustainable in the monopoly environment because some consumers (such as urban business customers) could be charged rates for local

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[21] Recommended Decision, 12 FCC Rcd at 472.

exchange and exchange access service that significantly exceeded the cost of providing service, and the rates paid by those customers would implicitly subsidize service provided by the same carrier to others. By adoption of the 1996 Act, Congress has provided for the development of competition in all telephone markets.[22] In a competitive market, a carrier that attempts to charge rates significantly above cost to a class of customers will lose many of those customers to a competitor. This incentive to entry by competitors in the lowest cost, highest profit market segments means that today's pillars of implicit subsidies – high access charges, high prices for business services, and the averaging of rates over broad geographic areas – will be under attack. New competitors can target service to more profitable customers without having to build into their rates the types of cross-subsidies that have been required of existing carriers who serve all customers.

18. By this Order, therefore, we will retain, with some limited modifications, the existing explicit high cost and low-income support programs until January 1, 1999, but make collection more equitable and nondiscriminatory and allow carriers other than ILECs to receive support; we will continue to coordinate with the states to determine the appropriate extent of universal service support for high cost areas as competition and related state decisions dictate; and we will fund universal service for eligible schools, libraries, and rural health care providers consistent with the statute. The total amount of federal high cost support (both implicit and explicit) will not decline materially, but will be restructured.

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[22] *See, e.g.*, 47 U.S.C. § 253.

19. Over time, it will be necessary to adjust the universal service support system to respond to competitive pressures and state decisions so that the support mechanisms are sustainable, efficient, explicit, and promote competitive entry. We expect to use both prescriptive (i.e., regulatory) and more permissive (i.e., market-based) approaches to complete this task. We expect that reform of both the universal service and access charge systems in accordance with Congress's direction and the principles set forth in the Act and this Order will achieve the following results:

- universal service support will be available for rural, insular, and high cost areas where local rates would otherwise become unaffordable for some users;

- state and federal universal service contributions will be collected equitably and non-discriminatorily from providers of telecommunication services, consistent with the statute's definitions;

- residential customers will be more likely to remain on the network by maintaining or improving today's subscribership rates, and others – particularly classrooms, libraries, and rural health care providers – who often lack network connections today will be connected;

- universal service will be sustainable in a competitive environment; this means both that the system of support must be competitively neutral and permanent, and that all support must be targeted as well as portable among eligible telecommunications carriers;

- universal service support will be specific, predictable, and sufficient to deliver service efficiently;

- originating and terminating per-minute access charges will be at forward-looking economic cost-based levels; and

- the total of the subscriber line charge and the presubscribed interexchange carrier (PIC) charge that we adopt today in our access reform proceeding, in combination with federal and state universal service support, will recover the deaveraged non-traffic sensitive costs of serving each customer;

20. Today's Order establishes the new federal universal service system that Congress and the Joint Board envisioned. Our continuing work with the states through the Joint Board process will ensure that this system is sustainable in a competitive marketplace, thus ensuring that universal service is available at rates that are "just, reasonable, and affordable" for all Americans.[23]

II. EXECUTIVE SUMMARY

A. Principles

21. Section 254(b) sets forth the principles that are to guide the Commission in establishing policies for the preservation of universal service. These principles include:

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[23] 47 U.S.C. § 254(b)(1).

(1) quality services should be available at just, reasonable, and affordable rates;[24]

(2) access to advanced telecommunications and information services should be provided in all regions of the Nation;[25]

(3) consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas;[26]

(4) all providers of telecommunications services should make an equitable and non-discriminatory contribution to the preservation and advancement of universal service;[27]

(5) there should be specific, predictable and sufficient [f]ederal and [s]tate mechanisms to preserve and advance universal service;[28] and

(6) elementary and secondary schools and classrooms, health care providers, and libraries should have access to advanced telecommunications services.[29]

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[24] 47 U.S.C. § 254(b)(1).

[25] 47 U.S.C. § 254(b)(2).

[26] 47 U.S.C. § 254(b)(3).

[27] 47 U.S.C. § 254(b)(4).

[28] 47 U.S.C. § 254(b)(5).

[29] 47 U.S.C. § 254(b)(6).

In addition, the Commission may consider such "additional principles" as the Commission and the Joint Board determine are necessary and appropriate for the protection of the public interest, convenience and necessity and are consistent with the Act.[30] In addition to the principles specified in section 254(b), we agree with the Joint Board and adopt its recommendation that "competitive neutrality" should be among the principles that guide the universal service support mechanisms and rules. We adopt this principle and the principles enumerated by Congress in section 254(b) to preserve and advance universal service while promoting the pro-competitive goals of the 1996 Act.

B. Definition of Universal Service

22. Section 254(c)(1) requires the Commission to establish a definition of telecommunications services that will be supported by universal service support mechanisms. Based on the principles embodied in section 254, and guided by the recommendation of the Joint Board, we find that the definition of supportable services includes: voice grade access to the public switched network, with the ability to place and receive calls; Dual Tone Multifrequency (DTMF) signaling or its functional equivalent; single-party service; access to emergency services, including in some instances, access to 911 and enhanced 911 (E911) services; access to operator services; access to interexchange services; access to directory assistance; and

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[30] 47 U.S.C. § 254(b)(7).

toll limitation services for qualifying low-income consumers. As recommended by the Joint Board, eligible carriers must offer each of the designated services in order to receive universal service support. We find that, consistent with the Joint Board's recommendation, a carrier that currently is unable to provide single-party service may petition its state commission to receive universal service support for a designated period of time while the carrier completes the network upgrades needed to offer single-party service. Further, based on the Joint Board's recognition that some carriers currently may be unable to provide access to E911 service and toll limitation services, carriers may receive, for a specified period of time, universal service support while completing network upgrades required for them to offer these services. In addition, all business and residential connections that are currently supported will continue to be supported until the forward-looking methodology for high cost companies is operational. Finally, as recommended by the Joint Board, we will convene a Federal-State Joint Board to review the definition of universal service on or before January 1, 2001.

C. Affordability

23. Based on the Joint Board's recommendation, we conclude that states should monitor rates and non-rate factors, such as subscribership levels, to ensure affordability. We agree with the Joint Board that there is a correlation between subscribership and affordability and we further agree that joint examination by the Commission and the states of the factors that may contribute to

low penetration is warranted in areas, such as insular areas, where subscribership levels are particularly low.

D. Carriers Eligible for Universal Service Support

24. We conclude that the plain language of section 214(e)(1) does not permit the Commission or the states to adopt additional criteria as prerequisites for designating carriers eligible telecommunications carriers. Therefore, consistent with the Joint Board's recommendation, we adopt the statutory criteria contained in section 214(e)(1) as the rules for determining whether a telecommunications carrier is eligible to receive universal service support. Pursuant to section 214(e), eligible carriers must offer and advertise all the services supported by federal universal service support mechanisms throughout their service areas using their own facilities or a combination of their own facilities and resale of another carrier's services. We interpret the term "facilities" in section 214(e)(1) to mean any physical components of the telecommunications network that are used in the transmission or routing of the services designated for support under section 254(c)(1). We conclude that our adoption of this interpretation strikes a reasonable balance between adopting a more expansive definition of "facilities," which would undermine the Joint Board's recommendation to exclude from eligibility a carrier offering universal service exclusively through resold services, and adopting a more restrictive definition of "facilities," which we fear would thwart competitive entry into high cost areas. In order to interpret the section 214(e) facilities requirement in a competitively neutral manner, we conclude that a

carrier that offers the federally supported services through the use of unbundled network elements, in whole or in part, satisfies the facilities requirement of section 214(e). We adopt the Joint Board's recommendation that eligible carriers not be required to offer the supported services wholly over their own facilities because the statute allows an eligible carrier to offer those services through a combination of its own facilities and resale. We also find, as did the Joint Board, that section 214(e) precludes an eligible carrier from offering the supported services solely through resale in light of the statutory requirement that a carrier provide universal service, at least in part, over its own facilities. Furthermore, consistent with the Joint Board's recommendation, we find that no additional measures are necessary to implement the provisions of section 254(e), which limit the purposes for which universal service funds may be used.

25. We agree with the Joint Board that the statute affords state commissions the primary responsibility for designating service areas served by non-rural carriers. We also concur in the Joint Board's finding, however, that states should exercise this authority in a manner that promotes the pro-competitive goals of the 1996 Act as well as the universal service principles of section 254. We therefore agree with the Joint Board that states should not designate service areas that are unreasonably large because unreasonably large service areas will discourage competitive entry by increasing the expenses associated with such entry. For similar reasons, and to promote competitive neutrality, we also recommend that state commissions not designate service areas that are based on

ILECs' study areas. The Act treats service areas served by rural telephone companies differently from non-rural service areas. Section 214(e)(5) requires a service area served by a rural telephone company to be that company's existing study area, unless the states and the Commission, after taking into account the findings of the Joint Board, establish a different definition. To minimize potential procedural delays associated with the federal-state cooperation that is required to alter the definition of a service area served by a rural carrier, we establish expedited procedures by which the definition of such an area may be changed in accordance with section 214(e)(5). We agree with the Joint Board that retaining the study areas of rural telephone companies as rural service areas is generally consistent with section 214(e)(5), the policy objectives underlying section 254, and with our decision to use a rural ILEC's embedded costs to calculate that company's support under the modified existing high cost mechanisms. We nevertheless encourage states to consider disaggregating a non-contiguous service area of a rural telephone company into service areas composed of the contiguous portions of that area because some wireless carriers may be unable to provide service in non-contiguous service areas. We conclude that the Joint Board correctly recommended that no additional regulations are necessary, at this time, to designate carriers to serve unserved areas. To assist us in monitoring the status of unserved areas, we encourage state commissions to submit to the Commission reports detailing the status of unserved areas in their states.

E. High Cost Support

26. Consistent with the Joint Board's recommendation, we find that a cost methodology based on forward-looking economic cost should be used to calculate the cost of providing universal service for high cost areas because it best reflects the cost of providing service in a competitive market for local exchange telephone service. We believe that a cost methodology can be designed based upon such consistent assumptions as economic depreciation, forward-looking cost of capital, and forward-looking outside plant cost, including reasonable profits. We agree with the Joint Board that the cost methodologies presented to us thus far are not sufficiently reliable to be used to determine universal service support at this time. Because input values that would significantly impact the model outputs, such as the cost of electronic switches and digital loop carrier devices, have never been provided to the Commission, we cannot accept the models before us. In addition, both models lack a compelling design for distributing customers in a particular geographic area, and thus, we cannot develop a reliable model based on the synthesis of the models before us. Consequently, we will issue a Further Notice of Proposed Rule Making (FNPRM) to establish a forward-looking universal service support mechanism based on forward-looking economic cost for non-rural carriers. We anticipate that we will adopt a forward-looking mechanism for non-rural carriers by August 1998, and that it will take effect on January 1, 1999. That mechanism will allow a state either to use the Commission's cost methodology or develop its own cost study, within the guidelines that we will establish, to determine the level of universal service

support for carriers in that state. Until the forward-looking mechanism takes effect on January 1, 1999, non-rural carriers will continue to receive high cost loop support and LTS based on the existing universal service mechanisms. As recommended by the state members of the Joint Board, rural carriers will continue to receive support based on their embedded cost using the current mechanisms with some modifications. We will continue to work with the Joint Board regarding the development of appropriate forward-looking economic cost mechanisms for rural carriers. As recommended by the Joint Board, we will also continue to explore the use of competitive bidding as a mechanism to provide universal service.

F. Support for Low-Income Consumers

27. We adopt the Joint Board's recommendations to make three broad categories of changes to the Lifeline and Link Up programs so that they better comport with our universal service principles and the 1996 Act's renewed concern for low-income consumers. First, we agree with the Joint Board's recommendation to expand Lifeline to make it available in all states, territories, and commonwealths of the United States, modify the state matching requirement, and increase the federal Lifeline support amount. We find that these modifications comply with the principles in sections 254(b)(1) and (3), respectively, that rates should be "affordable" and access should be provided to "low-income consumers" in all regions of the nation. Second, we adopt the Joint Board's

recommendation to make the contribution and distribution of low-income support competitively and technologically neutral by requiring equitable and nondiscriminatory contributions from all providers of interstate telecommunications services, consistent with sections 254(d) and (e), and allowing all eligible telecommunications carriers to receive support for offering Lifeline and Link Up service. Third, we adopt the Joint Board's recommendation to provide low-income consumers with access to certain services and policies.

28. Specifically, we agree with the Joint Board that Lifeline consumers should have access to the same services as those supported in rural, insular, and high cost areas: voice grade access to the public switched network, with the ability to place and receive calls; DTMF signaling or its functional equivalent; single-party service; access to emergency services, including in some circumstances, access to 911 and E911; access to operator services; access to interexchange services; and access to directory assistance. In determining the specific services to be provided to low-income consumers, we adopt the Joint Board's reasoning that section 254(b)(3) calls for access to services for low-income consumers in all regions of the nation, and that universal service principles may not be realized if low-income support is provided for service inferior to that supported for other subscribers. In addition, we agree with the Joint Board that Lifeline service should include toll-limitation services, at the customer's request, to the extent that carriers are capable of providing them. We agree with the Joint Board that toll-limitation services will help low-income consumers control their toll bills and consequently be

better able to maintain access to telecommunications services, as section 254(b)(3) envisions. We concur with the Joint Board's recommendation to prohibit the disconnection of local service for non-payment of charges incurred for toll calls. We are persuaded by the Joint Board's reasoning that such a rule will help improve subscribership among low-income consumers, based on studies indicating that disconnection for non-payment of toll charges is a significant cause of low subscribership among low-income consumers. We therefore believe that this rule advances the principles of section 254(b) that rates should be "affordable" and access to telecommunication services should be provided to "low-income consumers." We further find, as did the Joint Board, that local and toll services are distinct services, and therefore carriers providing toll service should take action against consumers who do not pay their toll bills. We also adopt the Joint Board's recommendation to prohibit carriers from requiring service deposits from Lifeline customers who elect toll blocking. Service deposits, which primarily serve to guard against uncollectible toll charges, deter subscribership among low-income consumers and thus run counter to the principle in section 254(b)(3) that low-income consumers should have access to telecommunications services. We therefore find, as did the Joint Board, that consumers who receive toll blocking, which bars the placement of toll calls, should be able to benefit from a rule prohibiting service deposits.

G. Support for Schools and Libraries

29. We concur with the Joint Board's recommendation to provide schools and libraries with discounts on all commercially available telecommunications services, Internet access, and internal connections. This program provides schools and libraries with the maximum flexibility to purchase the package of services they believe will meet their communications needs most effectively. We conclude that sections 254(c)(3) and 254(h)(1)(B) authorize us to permit eligible schools and libraries to receive telecommunications services, Internet access, and internal connections at discounted rates from telecommunications carriers. Because we share the Joint Board's preference that we foster competition from non-telecommunications carriers, we encourage those non-carrier providers to enter into partnerships or joint ventures with telecommunications carriers in order to provide services to schools and libraries. In addition, we adopt the Joint Board's recommendation to provide discounts for Internet access and internal connections provided by non-telecommunications carriers. We adopt this recommendation under the authority of sections 254(h)(2)(A) and 4(i).

30. We agree with the Joint Board's finding that fiscal responsibility compels us to require schools and libraries to seek competitive bids for all services eligible for section 254(h) discounts. Competitive bidding is the most efficient means for ensuring that schools and libraries are informed about all of the choices available to them. In addition, we agree with the Joint Board that the lowest corresponding price, defined for each telecommunications carrier bidding to serve a school or library as

the lowest price that carrier charges to similarly situated non-residential customers in its geographic service area for similar services, shall constitute the ceiling for that carrier's competitively bid pre-discount price for interstate rates. We would expect state commissions to require the same for intrastate rates. In areas in which there is only one bidder, that bidder's lowest corresponding price would constitute the pre-discount price.

31. We concur with the Joint Board's recommendation that we adopt discounts from 20 percent to 90 percent for all telecommunications services, Internet access, and internal connections, with the level of discounts correlated to indicators of poverty and high cost for schools and libraries. This approach satisfies section 254(h)(1)(B)'s directive that the discount be an amount that is "appropriate and necessary to ensure affordable access to and use of" the services eligible for the discount, and fulfills our statutory obligation to create specific, predictable, and sufficient universal service support mechanisms. We also adopt the Joint Board's recommendation to establish an annual cap of $2.25 billion on the amount of funds available to schools and libraries.

32. We agree with the Joint Board that all schools falling within the definition contained in the Elementary and Secondary Education Act of 1965 and meeting the criteria of section 254(h), whether public or private, shall be eligible for universal service support. In light of an amendment to section 254(h)(4), enacted in late 1996, we found it necessary to look anew at the definition of library and adopt a definition that is consistent with the directives of section 254(h). We, therefore, adopt the definition of library contained in the Library Services and

Technology Act for purposes of section 254(h), but we also conclude that a library's eligibility for universal service funding will depend on its funding as an independent entity. This independence requirement is consistent with both congressional intent and the expectation of the Joint Board that universal service support would flow to an institution of learning only if it is either an elementary or secondary school.

33. We agree with the Joint Board that schools and libraries should be permitted to participate in consortia for purposes of aggregating their demand with others. Because of concerns raised in comments received after adoption of the Recommended Decision that permitting large private sector firms to join with eligible schools and libraries to seek prices below tariffed rates could compromise both federal and state policies of non-discriminatory pricing, we adopt a slightly modified version of the Joint Board recommendation on consortia. We conclude, therefore, that eligible schools and libraries participating in consortia may receive universal service support only if such consortia are composed of other eligible schools and libraries, eligible health care providers, and ineligible public sector (governmental) members. Eligible schools and libraries participating in consortia that include ineligible private sector members will not be eligible to receive universal service discounts unless the pre-discount prices of any interstate services that such consortia receive from ILECs are generally tariffed rates. We conclude that this approach satisfies both the purpose and the intent of the Joint Board's recommendation because it should allow the consortia containing eligible schools and

libraries to aggregate sufficient demand to influence existing carriers to lower their prices and should promote efficient use of shared facilities. We also agree with the Joint Board's recommendation that we interpret section 254(h)(3) to restrict any resale whatsoever of services purchased pursuant to a section 254(h) discount.

34. We concur with the Joint Board's finding that Congress intended to require accountability on the part of schools and libraries. We agree, therefore, with the Joint Board's recommendation that eligible schools and libraries be required to: (1) conduct internal assessments of the components necessary to use effectively the discounted services they order; (2) submit a complete description of services they seek so that it may be posted for competing providers to evaluate; and (3) certify to certain criteria under penalty of perjury.

H. Support for Health Care Providers

35. Sections 254(c) and 254(h) add health care providers to the list of entities that may benefit from universal service support. Recognizing that section 254 requires that universal service support mechanisms be specific, predictable, and sufficient, we establish support for health care providers subject to a $400 million annual cap. Section 254(h)(1)(A) provides that a health care provider that serves persons who reside in rural areas shall receive telecommunications services necessary for the provision of health care services in a state at rates that are reasonably comparable to those charged for similar services in urban areas in that state. Because section 254(h)(1)(A) specifies that the calculation of the credit for carriers

providing the service is to be based on the difference between rates in "comparable rural areas," and the rates charged to the health care provider, we, consistent with the Joint Board recommendation, provide support under this section for telecommunications services for all public and not-for-profit health care providers located in rural areas. Any telecommunications service of a bandwidth capacity up to and including 1.544 Megabits per second (Mbps) that is necessary for the provision of health care services is eligible for support, but there are limits on the services that each rural health care provider may obtain. Telecommunications carriers must charge eligible rural health care providers a rate for each supported service that is no higher than the highest tariffed or publicly available commercial rate for a similar service in the closest city in the state with a population of 50,000 or more people, taking distance charges into account.

36. Section 254(h)(2)(A) directs the Commission to establish "competitively neutral rules to enhance, to the extent technically feasible and economically reasonable, access to advanced telecommunications and information services for all public and nonprofit health care providers." To meet the goals of this section, and, based on our review of comments filed in response to the Recommended Decision, we adopt mechanisms to provide support for limited toll-free access to an Internet service provider. Each health care provider that lacks toll-free access to an Internet service provider may receive the lesser of the toll charges incurred for 30 hours of access to an Internet service provider or $180 per month in toll charge credits for toll charges imposed for connecting to the Internet.

37. Carriers providing supported telecommunications services to health care providers will be entitled to treat the amount eligible for support as an offset against their annual universal service obligation and receive a reimbursement for any amount by which the support due the carrier exceeds the obligation in any one year. Non-telecommunications providers providing supported services to health care providers will receive direct reimbursement for the eligible amount.

I. Interstate Subscriber Line Charge/Carrier Common Line Charges

38. We adopt the Joint Board's conclusion that LTS must be removed from carrier common line (CCL) charges. This change will be effectuated in the access charge reform proceeding. Consistent with the Joint Board's recommendation, we provide for payments similar to LTS out of the new universal service support mechanisms to rural telephone companies that currently receive LTS or competitors that win subscribers from such carriers. Consistent with the Joint Board's recommendation, we maintain the current $3.50 cap on the SLC for primary residential and single-line business lines.

J. Administration of Support

39. Section 254(d) states that all carriers that provide interstate telecommunications services must contribute to universal service support mechanisms in an equitable and nondiscriminatory manner. To ensure that

all providers of similar services make the same contributions to universal service, we adopt the Joint Board's recommendation that all telecommunications carriers that provide interstate telecommunications services must contribute to the support mechanisms and we issue a list of examples of interstate telecommunications services. In addition, we find that the public interest requires providers of interstate telecommunications on a non-common carrier basis and payphone aggregators to contribute to the support mechanisms pursuant to the Commission's permissive authority over "other providers of interstate telecommunications." We adopt the Joint Board's recommendation that contributors whose contribution would be less than the administrator's administrative cost of collecting the contribution will be exempt from contribution and reporting requirements under the *de minimis* exemption contained in section 254(d).

40. Consistent with the Joint Board, we adopt a contribution assessment methodology that is competitively neutral and easy to administer. Contributions will be assessed against end-user telecommunications revenues, revenues derived from end users for telecommunications and telecommunications services, including SLCs. We adopt the Joint Board's recommendation that support for the programs for schools, libraries, and rural health care providers be assessed based on interstate and intrastate telecommunications revenues. Because the Joint Board did not issue a recommendation regarding the revenue base for the balance of the support mechanisms, we will maintain historic jurisdictional lines and will assess contributions for support for the high cost and

low-income programs on interstate telecommunications revenues.

41. Because the Joint Board did not address how contributors would recover their universal service contributions, we maintain historic jurisdictional lines and permit recovery of universal service contributions through the contributing carrier's interstate rates. For ILECs subject to price caps, we will permit universal service contributions to be added to the carrier's common line basket, and recovered in the same manner as common line charges.

42. Finally, we adopt the Joint Board's recommendation to appoint the National Exchange Carrier Association (NECA) the temporary administrator of the support mechanisms, subject to changes in NECA's governance that render it more representative of non-ILEC interests. Consistent with the Joint Board, we shall also create a Federal Advisory Committee to recommend a neutral, third-party permanent administrator of the support mechanisms. We require the administrators to administer the support mechanisms in a neutral and equitable manner, and to keep all support monies separate from all other funds under the control of the administrator or temporary administrator.

III. PRINCIPLES

A. Overview

43. Section 254(b) establishes six principles upon which the Joint Board and the Commission are to base

policies for the preservation and advancement of universal service. Section 254(b)(7) allows the Joint Board and the Commission to adopt additional principles necessary for the "protection of the public interest, convenience, and necessity."[68] In this section, consistent with the Joint Board's recommendation, we adopt the principles identified in section 254(b) and the additional principle of competitive neutrality. We concur with the Joint Board's recommendation "that policy on universal service should be a fair and reasonable balance of all of those principles identified in section 254(b) and the additional principle" of competitive neutrality.[69]

B. Background

44. Section 254(b) sets forth principles upon which the Joint Board and the Commission are to base policies for the preservation and advancement of universal service. These principles are:

> (1) QUALITY AND RATES. – Quality services should be available at just, reasonable, and affordable rates.
>
> (2) ACCESS TO ADVANCED SERVICES. – Access to advanced telecommunications and information services should be provided in all regions of the Nation.
>
> (3) ACCESS IN RURAL AND HIGH COST AREAS. – Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas,

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[68] 47 U.S.C. § 254(b)(7).

[69] Recommended Decision, 12 FCC Rcd at 101.

should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.

(4) EQUITABLE AND NONDISCRIMINATORY CONTRIBUTIONS. – All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service.

(5) SPECIFIC AND PREDICTABLE SUPPORT MECHANISMS. – There should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service.

(6) ACCESS TO ADVANCED TELECOMMUNICATIONS SERVICES FOR SCHOOLS, HEALTH CARE, AND LIBRARIES. – Elementary and secondary schools and classrooms, health care providers, and libraries should have access to advanced telecommunications services as described in subsection (h).

(7) ADDITIONAL PRINCIPLES. – Such other principles as the Joint Board and the Commission determine are necessary and appropriate for the protection of the public interest, convenience, and necessity and are consistent with this Act.[70]

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[70] 47 U.S.C. § 254(b).

45. In the Recommended Decision, the Joint Board recommended that the Commission's universal service policy "be a fair and reasonable balance" of all of the principles identified in section 254(b) and the additional principle of "competitive neutrality."[71] The Joint Board also recommended that the principle of competitive neutrality include the concept of technological neutrality "by allowing the marketplace to direct the development and growth of technology and avoiding endorsement of potentially obsolete services."[72] The Joint Board declined to recommend the adoption of additional principles designed to provide support to groups or services not specifically included under section 254.[73]

C. Discussion

46. Section 254(b)(7) permits the Commission to include among the principles specifically enumerated in section 254(b) "[s]uch other principles as the Joint Board and the Commission determine are necessary and appropriate for the protection of the public interest, convenience, and necessity and are consistent with this Act."[74] Pursuant to section 254(b)(7) and consistent with the Joint Board's recommendation, we establish "competitive neutrality" as an additional principle upon which we base policies for the preservation and advancement of universal service. In adopting this recommendation, we rely

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[71] Recommended Decision, 12 FCC Rcd at 101.

[72] Recommended Decision, 12 FCC Rcd at 101.

[73] Recommended Decision, 12 FCC Rcd at 102-103.

[74] 47 U.S.C. § 254(b)(7).

upon the Joint Board's reasoning, as set forth immediately below, and incorporate by reference the facts the Joint Board relied upon to support its recommendation.[75]

47. Consistent with the Joint Board's recommendation, we define this principle, in the context of determining universal service support, as:

> COMPETITIVE NEUTRALITY – Universal service support mechanisms and rules should be competitively neutral. In this context, competitive neutrality means that universal service support mechanisms and rules neither unfairly advantage nor disadvantage one provider over another, and neither unfairly favor nor disfavor one technology over another.

48. We agree with the Joint Board that, as a guiding principle, competitive neutrality is consistent with several provisions of section 254 including the explicit requirement of equitable and nondiscriminatory contributions.[76] We also note that section 254(h)(2) requires the Commission to establish competitively neutral rules relating to access to advanced telecommunications and information services for eligible schools, health care providers, and libraries.[77] The principle of competitive neutrality is

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[75] In adopting various other Joint Board recommendations, as discussed throughout this Order, we hereby expressly rely on the Joint Board's reasoning and incorporate by reference the facts the Joint Board relied upon to support those recommendations.

[76] *See* 47 U.S.C. § 254(d).

[77] *See* 47 U.S.C. § 254(h)(2).

also embodied in section 254(e)'s requirement that universal service support be explicit, section 254(f)'s requirement that state universal service contributions be equitable and nondiscriminatory, and section 214(e)'s requirement that any carrier can become an eligible telecommunications carrier if it meets certain statutory criteria.[78] In addition, we agree with the Joint Board that an explicit recognition of competitive neutrality in the collection and distribution of funds and determination of eligibility in universal service support mechanisms is consistent with congressional intent and necessary to promote "a pro-competitive, de-regulatory national policy framework."[79] We recognize, however, that given the complexities and diversity of the telecommunications marketplace it would be extremely difficult to achieve strict competitive neutrality. Our decisions here are intended to minimize departures from competitive neutrality, so as to facilitate a market-based process whereby each user comes to be served by the most efficient technology and carrier. We conclude that competitively neutral rules will ensure that such disparities are minimized so that no entity receives an unfair competitive advantage that may skew the marketplace or inhibit competition by limiting the available quantity of services or restricting the entry of potential service providers.

49. We concur in the Joint Board's recommendation that the principle of competitive neutrality in this context should include technological neutrality.[80] Technological

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[78] *See* 47 U.S.C. §§ 254(e) – (f), 214(e).

[79] Joint Explanatory Statement at 113.

[80] Recommended Decision, 12 FCC Rcd at 101.

neutrality will allow the marketplace to direct the advancement of technology and all citizens to benefit from such development. By following the principle of technological neutrality, we will avoid limiting providers of universal service to modes of delivering that service that are obsolete or not cost effective. The Joint Board correctly recognized that the concept of technological neutrality does not guarantee the success of any technology supported through universal service support mechanisms, but merely provides that universal service support should not be biased toward any particular technologies.[81] We anticipate that a policy of technological neutrality will foster the development of competition and benefit certain providers, including wireless, cable, and small businesses, that may have been excluded from participation in universal service mechanisms if we had interpreted universal service eligibility criteria so as to favor particular technologies. We also agree with the Joint Board's recommendation that the principle of competitive neutrality, including the concept of technological neutrality, should be considered in formulating universal service policies relating to each and every recipient and contributor to the universal service support mechanisms, regardless of size, status, or geographic location.[82]

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[81] For example, observing that wireless providers use spectrum shared among users to provide service, the Joint Board found that a wireless carrier provides the equivalent of single-party service when it provides a dedicated message path for the length of a party's particular transmission. Recommended Decision, 12 FCC Rcd at 112.

[82] Recommended Decision, 12 FCC Rcd at 101.

50. Commenters who express concern about the principle of competitive neutrality contend that Congress recognized that, in certain rural areas, competition may not always serve the public interest and that promoting competition in these areas must be considered, if at all, secondary to the advancement of universal service.[83] We believe these commenters present a false choice between competition and universal service. A principal purpose of section 254 is to create mechanisms that will sustain universal service as competition emerges. We expect that applying the policy of competitive neutrality will promote emerging technologies that, over time, may provide competitive alternatives in rural, insular, and high cost areas and thereby benefit rural consumers. For this reason, we reject assertions that competitive neutrality has no application in rural areas or is otherwise inconsistent with section 254.

51. We also find no evidence in the record or the legislative history to suggest that the lack of an express reference to competitive neutrality within the provisions of section 254(b) reflects a conscious determination by Congress to exclude this as an additional principle.[84] Rather, we agree with the Joint Board that promoting competition is an underlying goal of the 1996 Act and that the principle of competitive neutrality is consistent with that goal.[85] Accordingly, we conclude that the principle of competitive neutrality is "necessary and appropriate for the protection of the public interest" and is

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[83] *See, e.g.*, RTC comments at 33.

[84] Western Alliance comments at 10-11.

[85] Joint Explanatory Statement at 113.

"consistent with this Act" as required by section 254(b)(7).[86]

52. We agree with the Joint Board's recommendation that our universal service policies should strike a fair and reasonable balance among all of the principles identified in section 254(b) and the additional principle of competitive neutrality to preserve and advance universal service. Consistent with the recommendations of the Joint Board, we find that promotion of any one goal or principle should be tempered by a commitment to ensuring the advancement of each of the principles enumerated above.

53. We agree with the Joint Board's conclusion that Congress specifically addressed issues relating to individuals with disabilities in section 255[87] and, therefore, do not establish, at this time, additional principles related to individuals with disabilities for purposes of section 254. Section 255 requires all providers of telecommunications services and manufacturers of telecommunications equipment and customer premises equipment (CPE) to ensure that their equipment and services are accessible to individuals with disabilities, if readily achievable.[88] In the *Notice of Inquiry* adopted pursuant to section 255, the Commission sought comment on the implementation and enforcement of section 255.[89] The Commission also recently released a *Notice of Inquiry* seeking comment on

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[86] 47 U.S.C. § 254(b)(7).

[87] Recommended Decision, 12 FCC Rcd at 102.

[88] 47 U.S.C. § 255(b) – (c).

[89] Implementation of Section 255 of the Telecommunications Act of 1996, *Notice of Inquiry*, WT Docket No. 96-198, FCC 96-382 (rel. Sept. 19, 1996) *(255 NOI)*.

improving telecommunications relay service (TRS) for individuals with hearing and speech disabilities.[90] In particular, the *TRS NOI* sought comment on the length of TRS calls[91] and the effectiveness of existing rules to encourage carriers to distribute specialized customer premises equipment (SCPE) voluntarily at discounted rates or free of charge.[92] Although we are mindful of the commenters' concerns regarding the affordability of, and access to, telecommunications services by individuals with disabilities, we find that those concerns are more appropriately addressed in the context of the Commission's implementation of section 255.[93] Therefore, we do not adopt principles related to telecommunications users with disabilities in this proceeding.[94]

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[90] Telecommunications Relay Services, the Americans with Disabilities Act of 1990, and the Telecommunications Act of 1996, *Notice of Inquiry*, CC Docket No. 90-571, FCC 97-7 (rel. Jan. 14, 1997) (*TRS NOI*).

[91] *TRS NOI* at para. 41.

[92] *TRS NOI* at para. 43.

[93] We note that persons with disabilities who qualify under the low-income provisions of section 254(b)(3) will benefit from universal service support to low-income consumers. We recognize that access to health care and education is vital for all populations, and we anticipate that individuals with disabilities will be among those who will benefit from the provisions of section 254 regarding these services.

[94] *See* 47 U.S.C. §§ 225, 255. Section 225 relates to telecommunications services for hearing-impaired and speech-impaired individuals. We also note that interstate TRS, which allows persons with hearing or speech disabilities to communicate with persons who do not have such impairments through the use of a text telephone (TTY), is funded separately from universal service support mechanisms.

54. We have considered the requests to promote access to affordable telecommunications services to other groups and organizations, including minorities and community-oriented organizations,[95] but we decline to adopt these proposals as additional principles. Rather, consistent with the Joint Board's recommendation, we address the issue of access to affordable telecommunications services by only the particular groups identified by Congress in section 254: low-income consumers; eligible carriers serving rural, insular, and high cost areas; and eligible education and health care providers.[96] Moreover, with respect to ensuring affordable access to telecommunications services for minorities, we conclude below that the states and the Commission will monitor telephone subscribership levels for all Americans, including minorities, in an effort to determine whether we must take additional action to ensure affordable access to telecommunications services.[97] Accordingly, as recommended by the Joint Board, we decline at this time to adopt additional principles the purpose of which would be to extend universal service support to individuals, groups, or locations other than those identified in section 254.

55. Section 254(b)(4) provides for "equitable and nondiscriminatory contributions,"[98] and section 254(b)(5) provides that support mechanisms should be "specific

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[95] *See, e.g.*, Alliance for Community Media comments at 6-9; Public Advocates comments at 3-5.

[96] *See* section 254(b).

[97] *See infra* section V.

[98] 47 U.S.C. § 254(b)(4).

and predictable."[99] We find that these principles include the concept of "economic efficiency" to the extent that they promote competition through an open and competitively neutral marketplace, and we therefore find it unnecessary to adopt economic efficiency as an additional principle, as one commenter suggests.[100] We also find it unnecessary to designate access to the select services, such as interactive services, that commenters have proposed as additional principles for the Commission's universal service policies.[101] Instead, we consider, as discussed below, whether, consistent with the principles of the 1996 Act, these services should be included in the definition of universal service.[102] Finally, we reject proposals to establish a principle to minimize the size and growth of the universal service fund.[103] Although we take measures in this Order to maintain the size of the universal service support mechanisms at a level that is no higher than necessary to effectuate a comprehensive federal universal service policy, we note that section 254(b)(5) requires the Commission to ensure that there are "predictable and sufficient [f]ederal and [s]tate mechanisms to preserve and advance universal service."[104] In

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[99] 47 U.S.C. § 254(b)(5).

[100] GSA comments at 3.

[101] *See, e.g.*, Bar of New York comments at 3.

[102] *See infra* section IV.

[103] *See, e.g.*, Sprint PCS comments at 2-4; APC reply comments at 1; PCIA reply comments at 27.

[104] 47 U.S.C. § 254(b)(5). Consistent with the Joint Board's recommendation, we have sought to limit the services eligible for support to only those core services necessary to comply with the mandates of section 254. *See infra* section IV. We are also

accordance with this principle, we decline to adopt measures that may restrict our ability to comply with this mandate. Moreover, we anticipate that competition and market-based universal service techniques may eventually limit the size of the support mechanisms by providing affordable, cost-effective telecommunications services in many regions of the nation that are now dependent upon universal service support.

IV. DEFINITION OF UNIVERSAL SERVICE: WHAT SERVICES TO SUPPORT

A. Overview

56. Section 254(c)(1) requires the Joint Board to recommend, and the Commission to establish, the services that should be supported by federal universal service support mechanisms. Based on the principles embodied in section 254, and guided by the recommendation of the Joint Board, we define the "core" or "designated" services that will receive universal service support as: single-party service; voice grade access to the public switched network; Dual Tone Multifrequency ("DTMF")[105] signaling or its functional equivalent; access to emergency services including, in some circumstances,

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maintaining the indexed cap on high cost loop support for the period in which carriers will continue to receive high cost loop support based on the existing mechanisms. *See infra* section VII.

[105] DTMF facilitates the transportation of signaling through the network, shortening call set-up time.

access to 911 and Enhanced 911 ("E911");[106] access to operator services; access to interexchange service; access to directory assistance; and toll limitation services for qualifying low-income consumers, as described in section VIII. In order to receive universal service support, eligible carriers must offer each of the designated services. A carrier that currently is unable to provide single-party service may petition its state commission to permit this carrier to receive universal service support for a designated period of time while the carrier completes the network upgrades needed to offer single-party service. In addition, carriers currently incapable of providing access to E911 service and toll limitation services may, for a specific period of time, also receive universal service support while completing network upgrades required for them to offer these services.

57. All business and residential connections that are currently supported will continue to be supported prior to the operation of a forward-looking universal service support methodology. In assessing whether "quality services" are available, consistent with section 254(b)(1), because we will rely on existing data collection mechanisms, including data provided by states, we refrain from imposing additional data collection requirements at this time. Finally, the Commission will convene a Federal-State Joint Board to review the definition of universal service on or before January 1, 2001.[107]

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[106] Enhanced 911 or "E911" service enables emergency service personnel to identify the approximate location of the party calling 911.

[107] 47 U.S.C. § 254(c)(2).

B. Designated Services

1. Background

58. Section 254(c)(1) states that "[u]niversal service [is] an evolving level of telecommunications services that the Commission shall establish periodically under this section, taking into account advances in telecommunications and information technologies and services."[108] Section 254(c)(2) states that "[t]he Joint Board may, from time to time, recommend to the Commission modifications in the definition of the services that are supported by Federal universal service support mechanisms."[109] Moreover, the 1996 Act's legislative history provides that "[t]he Commission is given specific authority to alter the definition from time to time" in order to "take into account advances in telecommunications and information technology."[110]

59. Section 254(c)(1)(A)-(D) requires the Joint Board and the Commission to "consider the extent to which . . . telecommunications services" included in the definition of universal service:

> (1) are essential to education, public health, or public safety;
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> (2) have, through the operation of market choices by customers, been subscribed to by a substantial majority of residential customers;

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[108] 47 U.S.C. § 254(c)(1).

[109] 47 U.S.C. § 254(c)(2).

[110] Joint Explanatory Statement at 131.

(3) are being deployed in public telecommunications networks by telecommunications carriers; and

(4) are consistent with the public interest, convenience and necessity.[111]

The legislative history of this section instructs that "[t]he definition . . . should be based on a consideration of the four criteria set forth in the subsection."[112]

60. Section 254(b) establishes the principle that "consumers in all regions of the Nation . . . should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas. . . . "[113] The Joint Board recommended that all of the services and functionalities proposed in the NPRM be included in the general definition of services supported under section 254(c)(1).[114] The Joint Board also recommended that access to interexchange service – meaning the ability of a subscriber to place and receive

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[111] 47 U.S.C. § 254(c)(1)(A)-(D).

[112] Joint Explanatory Statement at 131.

[113] 47 U.S.C. § 254(b).

[114] Recommended Decision, 12 FCC Rcd at 112-115. The NPRM sought comment on whether the following services should be designated for universal service support: voice grade access to the public switched network, with the ability to place and receive calls; touch-tone; single-party service; access to emergency services, including access to 911 and E911 services; and access to operator services. NPRM at paras. 16, 18-22.

interexchange calls – be included as a supported service.[115] Finally, the Joint Board recommended supporting access to directory assistance, which the Board defined as the ability to place a call to directory assistance.[116]

2. Discussion

61. We generally adopt the Joint Board's recommendation and define the "core" or "designated" services that will be supported by universal service support mechanisms as: single-party service; voice grade access to the public switched network; DTMF signaling or its functional equivalent; access to emergency services; access to operator services; access to interexchange service; access to directory assistance; and toll limitation services for qualifying low-income consumers. In arriving at this definition, we have adopted the Joint Board's analysis and recommendation that, for purposes of section 254(c)(1), the Commission define "telecommunications services" in a functional sense, rather than on the basis of tariffed services. The record in this proceeding demonstrates ample support for the inclusion of the services, as defined in a functional sense, recommended by the Joint Board within the general definition of universal service.[117] We find, as the Joint Board concluded, that this definition of core universal services promotes competitive neutrality

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[115] Recommended Decision, 12 FCC Rcd at 121.

[116] Recommended Decision, 12 FCC Rcd at 122.

[117] *See, e.g.*, GSA comments at 8-9; ITI comments at 2; Teleport comments at 3; United Utilities comments at 2.

because it is technology neutral, and provides more flexibility for defining universal service than would a services-only approach.[118] We also adopt the Joint Board's analysis and finding that all four criteria enumerated in section 254(c)(1) must be considered, but not each necessarily met, before a service may be included within the general definition of universal service, should it be in the public interest.[119] We interpret the statutory language, particularly the word "consider," as providing flexibility for the Commission to establish a definition of services to be supported, after it considers the criteria enumerated in section 254(c)(1)(A)-(D). Thus, as discussed below, we conclude that the core services that we have designated to receive universal service support are consistent with the statutory criteria in section 254(c)(1).

62. *Single-Party Service.* We agree with and adopt the Joint Board's conclusion that single-party service is widely available and that a majority of residential customers subscribe to it, consistent with section 254(c)(1)(B).[120] Moreover, we concur with the Joint Board's conclusion that single-party service is essential to public health and safety in that it allows residential consumers access to emergency services without delay.[121] Single-party service also is generally consistent with the public interest, convenience, and necessity because, by eliminating the sharing required by multi-party service,

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[118] Recommended Decision, 12 FCC Rcd at 112.

[119] Recommended Decision, 12 FCC Rcd at 112.

[120] Recommended Decision, 12 FCC Rcd at 112.

[121] Recommended Decision, 12 FCC Rcd at 112.

single-party service significantly increases the consumer's ability to place calls irrespective of the actions of other network users and with greater privacy than party line service can assure. In addition, single-party service is being deployed in public telecommunications networks by telecommunications carriers. We adopt the Joint Board's finding that the term "single-party service" means that only one customer will be served by each subscriber loop or access line.[122] Eligible carriers must offer single-party service in order to receive support regardless of whether consumers choose to subscribe to single- or multi-party service. In addition, to the extent that wireless providers use spectrum shared among users to provide service, we find that wireless providers offer the equivalent of single-party service when they offer a dedicated message path for the length of a user's particular transmission. We concur with the Joint Board's recommendation not to require wireless providers to offer a single channel dedicated to a particular user at all times.[123]

63. *Voice Grade Access to the Public Switched Network.* As recommended by the Joint Board, we conclude that voice grade access includes the ability to place calls, and thus incorporates the ability to signal the network that the caller wishes to place a call.[124] Voice grade access also includes the ability to receive calls, and thus incorporates the ability to signal the called party that an incoming call

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[122] Recommended Decision, 12 FCC Rcd at 112.

[123] Recommended Decision, 12 FCC Rcd at 112.

[124] Recommended Decision, 12 FCC Rcd at 113.

is coming.[125] We agree that these components are necessary to make voice grade access fully beneficial to the consumer. We agree with and adopt the Joint Board's finding that, consistent with section 254(c)(1), voice grade access to the public switched network is an essential element of telephone service, is subscribed to by a substantial majority of residential customers, and is being deployed in public telecommunications networks by telecommunications carriers. In addition, we find voice grade access to be essential to education, public health, and public safety because it allows consumers to contact essential services such as schools, health care providers, and public safety providers. For this reason, it is also consistent with the public interest, convenience, and necessity. Accordingly, we adopt the Joint Board's recommended definition of voice grade access to the public switched network among the core services designated pursuant to section 254(c)(1).

64. We also adopt the Joint Board's recommendation that voice grade access should occur in the frequency range between approximately 500 Hertz and 4,000 Hertz for a bandwidth of approximately 3,500 Hertz.[126] We note that, although a substantial number of commenters favored supporting the Joint Board's definition of voice grade access,[127] few supported greater bandwidth

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[125] Consistent with the Joint Board's recommendation, we explicitly do not include call waiting, which is a discretionary service, within this definition.

[126] Recommended Decision, 12 FCC Rcd at 113.

[127] *See, e.g.*, GSA comments at 8-9; ITI comments at 2; Teleport comments at 3; United Utilities comments at 2.

capacity.[128] We are unpersuaded by Bar of New York's arguments in favor of including among the core services a higher level of telecommunications bandwidth capacity than was recommended by the Joint Board. Bar of New York notes the Joint Board's observation that services such as video-on-demand, medical imaging, two-way interactive distance learning and high definition television might require bandwidth capacity of 1.544 Mbps.[129] Although we conclude in sections X and XI below that certain higher bandwidth services should be supported under section 254(c)(3) for eligible schools, libraries, and rural health care providers,[130] we decline to adopt, pursuant to section 254(c)(1), a higher bandwidth than that recommended by the Joint Board. We conclude, except as further designated with respect to eligible schools, libraries and health care providers, that voice grade access, and not high speed data transmission, is the appropriate goal of universal service policies at this time

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[128] Bar of New York comments at 9-10; MFS comments at 5-11.

[129] Bar of New York comments at 9-10. *See also* MFS comments at 5-11 (recommending that universal service support mechanisms should support data transmissions of at least 1 Mbps).

[130] Pursuant to section 254(c)(3), the Commission may designate for support additional telecommunications services not included in the "core" services designated under section 254(c)(1) for schools, libraries, and health care providers. *See infra* sections X and XI for a discussion of services that we have designated for eligible schools, libraries, and health care providers may take at a discount and for which the carrier providing those services may receive compensation equal to that discount from universal service support mechanisms.

because we are concerned that supporting an overly expansive definition of core services could adversely affect all consumers by increasing the expense of the universal service program and, thus, increasing the basic cost of telecommunications services for all. As discussed above, voice grade access is subscribed to by a substantial majority of residential customers, and is being deployed in public telecommunications networks by telecommunications carriers. In contrast, the record in this proceeding does not demonstrate that the higher bandwidth services and data transmission capabilities advocated by Bar of New York and MFS are, at this time, necessary for the public health and safety and that a substantial majority of residential customers currently subscribe to these services.[131] Congress recognized, however, that the definition of services supported by universal service should advance with technology. Thus, we will periodically reexamine whether changes in technology, network capacity, consumer demand, and service deployment warrant a change in our definition of supported services.[132]

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[131] For example, recent data demonstrate that only .06 percent of residential connections are digital access lines, which are defined for purposes of the Commission's Automated Reporting and Management Information System ("ARMIS") as lines with capabilities of "64 Kpbs or 56 Kpbs or ISDN B channels or other equivalent communications channels." *ARMIS Operating Data Reports*, FCC Report 43-08 (rel. April 1, 1997) (as filed by reporting local exchange carriers).

[132] *See infra* section IV (discussing Joint Board's recommendation that the Commission convene a Federal-State Joint Board to review the definition of universal service on or before January 1, 2001).

65. *Support for Local Usage.* We agree with the Joint Board that the Commission should determine the level of local usage to be supported by federal universal service mechanisms and that the states are best positioned to determine the local usage component for purposes of state universal service mechanisms.[133] The Joint Board indicated strong record support for including a local usage component within the definition of universal service.[134] Further, we agree with the Joint Board that, in order for consumers in rural, insular, and high cost areas to realize the full benefits of affordable voice grade access, usage of, and not merely access to, the local network should be supported.[135]

66. We find, consistent with the Joint Board's conclusion, that we have the authority to support a certain portion of local usage, pursuant to the universal service principles adopted above.[136] In particular, section 254(b)(1) states that "[q]uality services should be available at just, reasonable, and affordable rates." As a result, ensuring affordable "access" to those services is not sufficient. We are unpersuaded by commenters who argue generally against supporting local usage,[137] because those

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[133] Recommended Decision, 12 FCC Rcd at 113.

[134] Recommended Decision, 12 FCC Rcd at 113.

[135] Recommended Decision, 12 FCC Rcd at 113. *See also* Ohio PUC reply comments at 2 (support for local usage is essential to make access to network truly beneficial for consumers).

[136] Recommended Decision, 12 FCC Rcd at 113.

[137] *See, e.g.*, Ameritech comments at 5 (states should support local usage through their own universal service mechanisms).

arguments ignore Congress's stated intent that the universal service policies shall be based, *inter alia*, on the principle that services should be available at affordable rates, as set forth in section 254(b)(1). As articulated by Ohio PUC, universal service must encompass the ability to use the network, including the ability to place calls at affordable rates.[138] We find that both access to and use of the public switched network at rates that are "just, reasonable and affordable," are necessary to promote the principles embodied in section 254(b)(1).

67. We are also concerned, however, that consumers might not receive the benefits of universal service support unless we determine a minimum amount of local usage that must be included within the supported services. An eligible carrier, particularly one that recovers a substantial portion of its costs through per-minute charges, could conceivably collect universal service support designed to promote affordable use of the network without, in turn, reducing the per-minute rates charged to its customers. Unless we are able to quantify an amount of local usage that must be provided without additional charge to the consumer by carriers receiving universal service support for serving rural, insular, and high costs areas, we believe there is a potential that the consumer would have to pay additional per-minute fees and would not receive the benefits universal service is designed to promote. We intend to consider this possible scenario in our Further Notice of Proposed Rulemaking ("FNPRM") on a forward-looking economic cost methodology, which will be issued by June 1997. As discussed

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[138] Ohio PUC reply comments at 2.

in section VII below, we are making various changes to the existing universal service support mechanisms – including making support portable to competing carriers – that will become effective on January 1, 1998.[139] The Commission will also separately seek further information regarding, for example, local usage, and local usage patterns, in order to determine the appropriate amount of local usage that should be provided by carriers receiving universal service support. We will, by the end of 1997, quantify the amount of local usage that carriers receiving universal service support will be required to provide.

68. At this time, we conclude that it is important to determine a minimum level of local usage in order to implement a forward-looking economic cost methodology, as described below in section VII. Without a prespecified amount of usage, it is not possible for forward-looking economic cost methodologies to determine accurately the cost of serving customers in high cost areas. The forward-looking economic cost methodologies require usage information to determine capacity requirements, such as switch size.[140]

69. In addition, determining and supporting a minimum level of usage for local service is important to further our principle of competitive neutrality, which includes technological neutrality. Different means of local service entry and competition can have markedly different cost structures. For instance, a wireline telephone

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[139] *See infra* section VII.D.

[140] *See infra* section VII.C.

system might have large initial "access" costs and relatively low "usage" or per-minute costs. In contrast, a wireless technology might have moderate "access" costs but high per-minute costs than a wireline network. In such a situation, merely supporting "access" without supporting a certain amount of local usage could favor unfairly a particular technology. This result may violate our principle of competitive neutrality.

70. Further, the Joint Board anticipated that competitive bidding may become an efficient method of determining universal service support amounts.[141] Defining minimum levels of usage is critical to the construction of a competitive bidding system for providing universal service to high cost areas. An auction for only the "access" portion of providing local service would be neither competitively nor technologically neutral, because competitors and technologies with low "access" costs yet high per-minute costs would be unduly favored in such an auction. This could result in awarding universal service support to a less efficient technology, which is the precise result that a competitive bidding system is meant to avoid. In addition, a carrier with low access costs could then charge high per-minute rates to consumers, which would increase consumers' overall bills, rather than reducing them, as is the expected result of competition. Such a result is not consistent with the principle in section 254(b)(1) that these "services" are to be "affordable."

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[141] *See* Recommended Decision, 12 FCC Rcd at 266. *See also infra* section VII.

71. *DTMF Signaling*. The Joint Board recommended including DTMF signaling or its digital functional equivalent among the supported services, and we adopt this recommendation.[142] We find that the network benefit that emanates from DTMF signaling, primarily rapid call set-up, is consistent with the public interest, convenience, and necessity, pursuant to section 254(c)(1)(D). Although consumers do not elect to subscribe to DTMF signaling, *per se*, we find, as the Joint Board concluded, that DTMF signaling provides network benefits, such as accelerated call set-up, that are essential to a modern telecommunications network. In addition, we agree with NENA's characterization of DTMF signaling as a potential life- and property-saving mechanism because it speeds access to emergency services. Thus, we find that supporting DTMF signaling is essential to public health and public safety, consistent with section 254(c)(1)(A), and is being deployed in public telecommunications networks by telecommunications carriers, consistent with section 254(c)(1)(C). We also adopt the Joint Board's conclusion that other methods of signaling, such as digital signaling, can provide network benefits equivalent to those of DTMF signaling. In particular, we note that wireless carriers use out-of-band digital signaling mechanisms for call set-up, rather than DTMF signaling. Consistent with the principle of competitive neutrality, we find it is appropriate to support out-of-band digital signaling mechanisms as an alternative to DTMF signaling.[143]

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[142] *See* Recommended Decision, 12 FCC Rcd at 114.

[143] Hereafter, we refer to both DTMF signaling and its functional equivalent, digital signaling, as "DTMF signaling."

Accordingly, we include DTMF signaling and equivalent digital signaling mechanisms among the services supported by federal universal service mechanisms.

72. *Access to Emergency Services.* In addition, we concur with the Joint Board's conclusion that access to emergency services, including access to 911 service, be supported by universal service mechanisms.[144] We agree with the Joint Board's conclusion that access to emergency service i.e., the ability to reach a public emergency service provider, is "widely recognized as essential to . . . public safety," consistent with section 254(c)(1)(A).[145] Due to its obvious public safety benefits, including access to emergency services among the core services is also consistent with the public interest, convenience, and necessity. Further, consistent with the Joint Board's recommendation and NENA's comments in favor of supporting access to 911 service, we define access to emergency services to include access to 911 service.[146] Noting that nearly 90 percent of lines today have access to 911 service capability, the Joint Board found that access to 911 service is widely deployed and available to a majority of residential subscribers.[147] For these reasons, we include telecommunications network components necessary for access to emergency services, including access to 911, among the supported services.

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[144] *See* Recommended Decision, 12 FCC Rcd at 114.

[145] *See* Recommended Decision, 12 FCC Rcd at 114.

[146] Recommended Decision, 12 FCC Rcd at 114; NENA comments at 1.

[147] Recommended Decision, 12 FCC Rcd at 114.

73. We also include the telecommunications network components necessary for access to E911 service among the services designated for universal service support. Access to E911 is essential to public health and safety because it facilitates the determination of the approximate geographic location of the calling party. We recognize, however, that the Commission does not currently require wireless carriers to provide access to E911 service.[148] As set forth in the Commission's *Wireless E911 Decision*, access to E911 includes the ability to provide Automatic Numbering Information ("ANI"),[149] which permits that the PSAP have call back capability if the call is disconnected, and Automatic Location Information

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[148] As the Joint Board recognized, cellular, broadband Personal Communications Service (PCS), and certain Specialized Mobile Radio (SMR) carriers are currently in a transition period during which they are making the technical upgrades needed to offer access to E911. Recommended Decision, 12 FCC Rcd at 114. These carriers need to complete the upgrades necessary to provide all of the E911 services specified in the Commission's Report and Order by 2001. It is significant, however, that a wireless carrier's obligation to provide such E911 services applies only if (1) a locality has implemented E911 service, i.e., if a public safety answering point (PSAP) capable of receiving and utilizing the data elements associated with the E911 services has requested that the carrier provide E911 service and (2) if a mechanism for the recovery of costs relating to the provision of such services is in place. Revision of the Commission's Rules to Ensure Compatibility with Enhanced 911 Emergency Calling Systems, CC Docket No. 94-102, *Report and Order and Further Notice of Proposed Rulemaking*, FCC 96-264 (rel. July 26, 1996), recon. pending (*Wireless E911 Decision*).

[149] *Wireless E911 Decision* at paras. 63-66.

("ALI"),[150] which permits emergency service providers to identify the geographic location of the calling party. We recognize that wireless carriers are currently on a timetable, established in the *Wireless E911 Decision*, for implementing both aspects of access to E911.[151] For universal service purposes, we define access to E911 as the capability of providing both ANI and ALI. We note, however, that wireless carriers are not required to provide ALI until October 1, 2001.[152] Nevertheless, we conclude that, because of the public health and safety benefits provided by access to E911 services the telecommunications network components necessary for such access will be supported by federal universal service mechanisms for those carriers that are providing it.[153] We recognize that wireless providers will be providing access to E911 in the future to the extent that the relevant locality has implemented E911 service. In addition, because the *Wireless E911 Decision* establishes that wireless carriers are

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[150] ALI is a requirement under which "covered carriers must achieve the capability to identify the latitude and longitude of a mobile unit making a 911 call, within a radius of no more than 125 meters in 67 percent of all cases." *Wireless E911 Decision* at para. 71.

[151] *Wireless E911 Decision* at para. 63, 68.

[152] *Wireless E911 Decision* at para. 68.

[153] As set forth below, we adopt a procedure that permits otherwise eligible carriers seeking universal service support to receive a grant of additional time for complying with our general requirement that eligible carriers provide access to E911, when the relevant locality has implemented E911 service, in order to receive universal service support. *See* discussion below in section IV.C.2 addressing feasibility issues associated with providing access to 911 and E911 services.

required to provide access to E911 only if a mechanism for the recovery of costs relating to the provision of such services is in place, there is at least the possibility that wireless carriers receiving universal service support will be compensated twice for providing access to E911.[154] We intend to explore whether the possibility is in fact being realized and, if so, what steps we should take to avoid such over-recovery in a Further Notice of Proposed Rulemaking.

74. Consistent with the Joint Board's recommendation, we support the telecommunications network components necessary for access to 911 service and access to E911 service, but not the underlying services themselves, which combine telecommunications service and the operation of the PSAP and, in the case of E911 service, a centralized database containing information identifying approximate end user locations.[155] As noted by the Joint Board and commenters, the telecommunications network represents only one component of 911 and E911 services; local governments provide the PSAP and generally support the operation of the PSAP through local tax revenues.[156] We conclude that both 911 service and E911 service include information service components that cannot be supported under section 254(c)(1), which describes

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[154] *Wireless E911 Decision* at para. 89.

[155] Recommended Decision, 12 FCC Rcd at 114.

[156] Recommended Decision, 12 FCC Rcd at 114. *See also* Ameritech NPRM comments at 7 (support should be provided for transmission facility that connects subscriber to location manned by public safety personnel but not for underlying service because local taxes generally support underlying service).

universal service as "an evolving level of telecommunications services."[157] Accordingly, we include only the telecommunications network components necessary for access to 911 and E911 services among the services that are supported by federal universal service mechanisms.

75. *Access to Operator Services.* In addition, we adopt the Joint Board's recommendation to include access to operator services in the general definition of universal service.[158] As the Joint Board concluded, access to operator services is widely deployed and used by a majority of residential customers.[159] For purposes of defining the core section 254(c)(1) services and consistent with the Joint Board's recommendation, we base our definition of "operator services" on the definition the Commission used to define the duties imposed upon LECs by section 251(b)(3), namely, "any automatic or live assistance to a consumer to arrange for billing or completion, or both, of a telephone call."[160] We reject CWA's argument that access to operator services should include "initial contact

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[157] 47 U.S.C. § 254(c)(1).

[158] Recommended Decision, 12 FCC Rcd at 115.

[159] Recommended Decision, 12 FCC Rcd at 115.

[160] *Local Competition Second Report and Order* at paras. 13, 110. We explicitly do not, however, include busy line verification and emergency interrupt within the definition of operator services for universal service purposes because the record does not support including these functions. *Cf. Local Competition Second Report and Order* at para. 111 (concluding that busy line verification and emergency interrupt are forms of operator services).

with a live operator," which, it contends, is "indispensable for users in public health or safety emergencies."[161] Contrary to the suggestion of CWA, there is no evidence on the record to suggest that automated systems provide inadequate access to operator services for consumers in emergency situations. We also do not require initial contact with a live operator for purposes of operator services because we expect that most consumers will more appropriately rely upon their local 911 service in an emergency situation. To the extent that access to operator services enables callers to place collect, third-party billed, and person-to-person calls, among other things, we find that such access may be essential to public health and is consistent with the public interest, convenience, and necessity.

76. *Access to Interexchange Service.* We adopt the Joint Board's recommendation to include access to interexchange service among the services supported by federal universal service mechanisms.[162] We conclude that access to interexchange service means the use of the loop, as well as that portion of the switch that is paid for by the end user, or the functional equivalent of these network elements in the case of a wireless carrier, necessary to access an interexchange carrier's network.[163] This

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[161] CWA reply comments at 4.

[162] Recommended Decision, 12 FCC Rcd at 121-122.

[163] For an interexchange call, the IXC rather than the end user currently pays for switching costs. To the extent that, under the access charge rate structure rules we adopt today, the end user may pay for a portion of the costs of line ports used to connect the loop to the local switch, which is used to access the IXC's network, that portion will be supported by universal

decision is consistent with the principle set forth in section 254(b)(3) that "consumers . . . should have access to telecommunications and information services including interexchange services." In addition, we agree with the Joint Board that the majority of residential customers currently have access to interexchange service, thus satisfying a criterion set forth in section 254(c)(1)(B).[164] Access to interexchange service also is widely deployed in public telecommunications networks by telecommunications carriers. Further, as observed by the Joint Board and commenters, access to interexchange service is essential for education, public health, and public safety, particularly for customers who live in rural areas and require access to interexchange service to reach medical and emergency services, schools, and local government offices.[165] For these reasons, access to interexchange service also meets the public interest, convenience, and necessity criterion of section 254(c)(1)(D).

77. Regarding GCI's argument that interexchange service should not be supported because it is a competitive service, we emphasize that universal service support will be available for access to interexchange service, but not for the interexchange or toll service.[166] We find that the record does not support including toll service among the services designated for support, although, as discussed in section V below, we find that the extent to

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service support mechanisms. *See Access Charge Reform Order* at section III.B.

[164] Recommended Decision, 12 FCC Rcd at 122.

[165] Recommended Decision, 12 FCC Rcd at 122.

[166] GCI reply comments at 10-11.

which rural consumers must place toll calls to reach essential services should be considered when assessing affordability. Nevertheless, universal service should not be limited only to "non-competitive" services. One of the fundamental purposes of universal service is to ensure that rates are affordable regardless of whether rates are set by regulatory action or through the competitive marketplace. GCI's argument implies that, if there were multiple carriers competing to provide, for example, basic dialtone service at $1000 per month, there could be no universal service support because the price was set through competition. Such a result would be inconsistent with Congress's intentions to preserve and advance universal service in adopting section 254. We note that section 254(k), which forbids telecommunications carriers from using services that are not competitive to subsidize competitive services, is not inconsistent with our conclusion that it is permissible to support competitive services.[167]

78. Consistent with the Joint Board's recommendation, we do not include equal access to interexchange service among the services supported by universal service mechanisms.[168] Equal access to interexchange service permits consumers to access the long distance carrier to which the consumer is presubscribed by dialing a 1+ number. As discussed below in section VI, including equal access to interexchange service among the services supported by universal service mechanisms would

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[167] *See* 47 U.S.C. § 254(k).

[168] Recommended Decision, 12 FCC Rcd at 122.

require a Commercial Mobile Radio Service (CMRS) provider to provide equal access in order to receive universal service support. We find that such an outcome would be contrary to the mandate of section 332(c)(8), which prohibits any requirement that CMRS providers offer "equal access to common carriers for the provision of toll services."[169] Accordingly, we decline to include equal access to interexchange service among the services supported under section 254(c)(1).

79. Contrary to Ameritech's argument, competitive neutrality does not require that, in areas where incumbent LECs are required to offer equal access to interexchange service, other carriers receiving universal service support in that area should also be obligated to provide equal access.[170] As discussed in section VI below, statutory and policy considerations preclude us from imposing "symmetrical" service obligations on all eligible carriers, including the obligation to provide equal access to interexchange service, as a condition of eligibility under section 214(e). We note that the Commission has not required CMRS providers to provide dialing parity[171]

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[169] Section 332(c)(8) states that CMRS providers shall not be "required to provide equal access to common carriers for the provision of toll service." 47 U.S.C. § 332(c)(8).

[170] *See infra* section IV.

[171] The term "dialing parity" means "that a person that is not an affiliate of a local exchange carrier is able to provide telecommunications services in such a manner that customers have the ability to route automatically, without the use of any access code, their telecommunications to the telecommunications services provider of the customer's designation from among two or more telecommunications services providers (including such local exchange carrier)." 47 U.S.C. § 153(15).

to competing providers under section 251(b)(3) because the Commission has not yet determined that any CMRS provider is a LEC.[172] We seek to implement the universal service provisions of section 254 in a manner that is not "biased toward any particular technologies," consistent with the Joint Board's recommendation.[173] In light of the provision of section 332(c)(8) stating that non-LEC CMRS providers are statutorily exempt from providing equal access[174] and because the Commission has not determined that any CMRS providers should be considered LECs,[175] we find that supporting equal access would

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[172] *See Local Competition Second Report and Order* at para. 29. Pursuant to section 3(26), the term "local exchange carrier . . . does not include a person insofar as such person is engaged in the provision of a commercial mobile service under section 332(c), except to the extent that the Commission finds that such service should be included in the definition of such term." In adopting rules to implement the dialing parity obligations of section 251(b)(3), the Commission expressly concluded that, for purposes of that section, CMRS providers are not LECs. *Local Competition Second Report and Order* at para. 29. Under section 332(c)(8), if, in the future, the Commission determines that CMRS providers should be treated as LECs, it may then "prescribe regulations to afford subscribers unblocked access to the provider of telephone toll services of the subscriber's choice through the use of a carrier identification code assigned to such provider or other mechanism" if the Commission determines that "subscribers to [commercial mobile services] are denied access to the provider of telephone toll services of the subscriber's choice, and that such denial is contrary to the public interest, convenience, and necessity."

[173] Recommended Decision, 12 FCC Rcd at 101.

[174] 47 U.S.C. § 332(c)(8).

[175] *Local Competition Second Report and Order* at para. 29.

undercut local competition and reduce consumer choice and, thus, would undermine one of Congress's overriding goals in adopting the 1996 Act.[176] Accordingly, we do not include equal access to interexchange carriers in the definition of universal service at this time.

80. *Access to Directory Assistance and White Pages Directories.* We also adopt the Joint Board's recommendation to include access to directory assistance, specifically, the ability to place a call to directory assistance, among the core services pursuant to section 254(c)(1).[177] Access to directory assistance enables customers to obtain essential information, such as the telephone numbers of government, business, and residential subscribers. We agree with and adopt the Joint Board's analysis and conclusion that directory assistance is used by a substantial majority of residential customers, is widely available, is essential for education, public health, and safety, and is consistent with the public interest, convenience, and necessity.[178] Accordingly, we conclude that providing universal service support for access to directory assistance is consistent with the statutory criteria of section 254(c)(1).

81. We further agree with the Joint Board's recommendation not to support white pages directories and

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[176] *See* Joint Explanatory Statement at 113 ("to provide for a pro-competitive, de-regulatory national policy framework").

[177] Recommended Decision, 12 FCC Rcd at 122.

[178] Recommended Decision, 12 FCC Rcd at 122-23.

listings.[179] We concur with the Joint Board's determination that white pages listings are not "telecommunications services" as that term is defined in the Act.[180] We disagree with West Virginia Consumer Advocate's assertion that it is inconsistent to support access to directory assistance, but not white pages directory listings.[181] As the Joint Board recognized, unlike white pages directories and listings, access to directory assistance is a functionality of the loop and, therefore, is a service in the functional sense.[182] While we conclude that white pages directories do not meet the statutory requirements of section 254(c)(1), we find that they provide consumers with valuable information, encourage usage of the network, and may facilitate access to telecommunications and information services.[183] For these reasons, we encourage carriers to continue to make white pages directories available to consumers.

82. *Toll Limitation Services.* Additionally, we include the toll limitation services for qualifying low-income consumers, as discussed more fully below in section VIII, among those that will be supported pursuant to section

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[179] A white pages directory is a compilation of the individual white pages listings.

[180] *See* 47 U.S.C. § 153(46).

[181] West Virginia Consumer Advocate comments at 2. *See also* Ohio PUC comments at 5; CWA reply comments at 4.

[182] Recommended Decision, 12 FCC Rcd at 122.

[183] In addition, we note that section 271(c)(2)(B)(viii) requires that BOCs, prior to providing interLATA service, provide white pages directory listings for customers of competing carriers' telephone exchange service. 47 U.S.C. § 271(c)(2)(B)(viii).

254(c). In the Recommended Decision, the Joint Board concluded that Lifeline customers should have access to toll control services, at the customer's option, and at no charge, based on data showing that uncontrollable toll charges were a major factor in low subscribership levels among low-income consumers.[184] Although the record does not indicate that a majority of residential subscribers currently subscribe to toll limitation services, the Joint Board found that telecommunications carriers are deploying toll limitation services in public telecommunications networks, consistent with section 254(c)(1)(C).[185] We find that including these services within the supported services is essential to the public health and safety because, as discussed in section VIII below, toll limitation services will help prevent subscribership levels for low-income consumers from declining. Thus, we find that toll limitation services will promote access to the public switched network for low-income consumers[186] and, therefore, are in the public interest, consistent with the criteria of section 254(c)(1).[187]

83. *Access to Internet Services.* We agree with the Joint Board's determination that Internet access consists

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[184] Recommended Decision, 12 FCC Rcd at 285.

[185] Recommended Decision, 12 FCC Rcd at 286. *See infra* section VIII.

[186] *See infra* section VIII for a discussion of the increased penetration rates in areas in which Lifeline and Link Up programs are available for low-income consumers.

[187] *See* 47 U.S.C. § 254(c)(1).

of more than one component.[188] Specifically, we recognize that Internet access includes a network transmission component, which is the connection over a LEC network from a subscriber to an Internet Service Provider, in addition to the underlying information service. We also concur with the Joint Board's observation that voice grade access to the public switched network usually enables customers to secure access to an Internet Service Provider, and, thus, to the Internet.[189] We conclude that the information service component of Internet access cannot be supported under section 254(c)(1), which describes universal service as "an evolving level of telecommunications services."[190] Furthermore, to the extent customers find that voice grade access to the public switched network is inadequate to provide a sufficient telecommunications link to an Internet service provider, we conclude that such higher quality access links should not yet be included among the services designated for support pursuant to section 254(c)(1). We find that a network transmission component of Internet access beyond voice grade access should not be supported separately from voice grade access to the public switched network because the record does not indicate that a substantial majority of residential customers currently subscribe to Internet access by using access links that provide higher quality than voice grade

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[188] Recommended Decision, 12 FCC Rcd at 323. Internet access consists of both a network transmission component and an information service component.

[189] Recommended Decision, 12 FCC Rcd at 123.

[190] *See infra* section X for a discussion of information services.

access.[191] In addition, although access to Internet services offers benefits that contribute to education and public health, we conclude that it is not *"essential* to education, public health, or public safety" as set forth in section 254(c)(1)(A).[192] We conclude that our decision not to support this component is consistent with the Joint Board's general finding that support beyond that provided for voice grade access to the public switched network is not warranted at this time.[193] Under the more expansive authority granted in section 254(h), however, we agree that supporting Internet access under that section is consistent with Congress's intent to support Internet access for eligible schools, libraries, and rural health care providers.[194] Finally, just as the Joint Board concluded that increasing demand for Internet service will provide consumers with broader accessibility to Internet service

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[191] Based on recent surveys, we estimate that approximately 6 percent of all residential Internet subscribers have access faster than dial-up access. *See* "US On-Line Population Reaches 47 Million – Intelliquest Survey Results," Internet IT Informer, February 2, 1997 (concluding that 22.3 million people in the United States primarily access the Internet from home); "Commercial Internet Exchange Internet Service Provider Study," March 1997, submitted with Commercial Internet Exchange comments in CC Docket 96-263 (March 24, 2997 [sic]) (indicating that 94 percent of residential Internet users use dial-up access, five percent use Integrated Services Digital Network (ISDN), and one percent use other, presumably higher-speed, services to access the Internet).

[192] 47 U.S.C. § 254(c)(1)(A) (emphasis added).

[193] Recommended Decision, 12 FCC Rcd at 123.

[194] *See infra* section X.

providers,[195] we anticipate that the demand for Internet service will cause carriers to offer higher bandwidth services and data rates for residential customers.

84. *Other Services.* We conclude that, at this time, no other services that commenters have proposed to include in the general definition of universal service substantially meet the criteria set forth in section 254(c)(1).[196] We emphasize that this section also defines universal service as "evolving" and, therefore, as described below, the Commission will review the services supported by universal service mechanisms no later than January 1, 2001. In addition, as discussed below in section III, we find that the issues relating to the telecommunications needs of individuals with disabilities, including accessibility and affordability of services, will be addressed in the context of the Commission's implementation of section 255.[197]

85. Moreover, we disagree with the view expressed by Benton that universal service should be defined by transport and termination requirements rather than services.[198] As discussed above, we concur with the Joint Board's recommendation that, for purposes of section 254(c)(1), the Commission define telecommunications services in a functional sense. We find that Benton's concerns that this approach will favor "carriers traditionally

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[195] Recommended Decision, 12 FCC Rcd at 123.

[196] We address the proposal of Catholic Conference with respect to supporting voice messaging services for individuals without residences in section VIII in our discussion of support for low-income consumers.

[197] *See supra* section III.

[198] Benton comments at 2.

associated with" the network elements needed to provide the designated services are unfounded.[199] Contrary to Benton's contention, the record does not contradict the Joint Board's conclusion that none of the designated services creates a barrier to entry for potential new competing carriers or otherwise impedes the ability of wireless and other telecommunications carriers to provide universal service.[200]

86. Further, we do not adopt the proposal advocated by GTE and others to require eligible carriers to offer the designated services on an unbundled basis.[201] As discussed more fully below in section VI, based on our analysis of section 214(e), we conclude that the statutory language set forth in that section prevents the Commission and the states from imposing on eligible carriers requirements that are not included in the statutory language.[202] Even assuming that section 214(e) permitted the Commission to impose requirements on eligible carriers, we would not be inclined to adopt GTE's proposal because we find that, in areas in which there is no competition, states are charged with setting rates for local services and, where competing carriers are offering universal services, consumers would choose to receive service from the carrier that offers the service package that best suits the consumer's needs.

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[199] Benton comments at 2.

[200] Recommended Decision, 12 FCC Rcd at 115.

[201] GTE comments at 16. *See also* Ameritech comments at 9 n.15; TCA comments at 3-4.

[202] 47 U.S.C. § 214(e).

87. Moreover, we are mindful of the concern expressed by commenters[203] that an overly broad definition of universal service might have the unintended effect of creating a barrier to entry for some carriers because, as discussed below in section IV.C.2, carriers must provide each of the core services in order to be eligible for universal service support. We concur with the Joint Board's conclusion that conditioning a carrier's eligibility for support upon its provision of the core services will not impose an anti-competitive barrier to entry.[204] We note that other services proposed by commenters, at a later time, may become more widely deployed than they are at present, or otherwise satisfy the statutory criteria by which we and the Joint Board are guided. When reviewing the definition of universal service, as anticipated by section 254(c)(2), the Commission and the Joint Board, after considering the implications for competition, may find that additional services proposed by commenters should be included in our list of core services.

C. Feasibility of Providing Designated Services

1. Background

88. Section 214(e)(1)(A) requires eligible carriers to "offer the services that are supported by [f]ederal universal service support mechanisms."[205] The Joint Board recommended that, pursuant to section 214(e), carriers designated as eligible telecommunications providers

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[203] *See, e.g.*, CTIA comments at 9.

[204] Recommended Decision, 12 FCC Rcd at 128.

[205] 47 U.S.C. § 214(e)(1)(A).

should be required to offer all of the services designated for universal service support.[206] Recognizing that some incumbent LECs may currently be unable to provide single-party service, however, the Joint Board recommended that state commissions be permitted to grant a transition period to otherwise eligible carriers that initially are unable to provide single-party service but only upon a finding that "exceptional circumstances" warrant a transition period.[207] In addition, the Joint Board recommended supporting access to E911 service, to the extent that eligible carriers currently are capable of providing such access and the relevant locality has chosen to implement E911 service.[208] Similarly, the Joint Board recommended that toll blocking or control services should be supported when provided to eligible low-income consumers, to the extent that eligible carriers are technically capable of providing these services.[209]

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[206] Recommended Decision, 12 FCC Rcd at 128.

[207] Recommended Decision, 12 FCC Rcd at 129.

[208] Recommended Decision, 12 FCC Rcd at 130.

[209] Recommended Decision, 12 FCC Rcd at 130.

2. Discussion

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do not constitute a tax.[2064] Therefore, contrary to Celpage's arguments, requiring paging companies to contribute to the support mechanisms does not present constitutional problems. Some commenters also argue that carriers ineligible to receive support should be allowed to make reduced contributions to universal service.[2065] Because section 254(d) states that "every telecommunications carrier that provides interstate telecommunications services" must contribute to universal service and does not limit contributions to "eligible carriers," we agree with the Joint Board and reject these arguments. Thus, we find that the *de minimis* exemption cannot and should not be interpreted to allow reduced contributions or contribution exemptions for ineligible carriers.

E. Scope of the Commission's Authority Over the Universal Service Support Mechanisms

1. Overview

806. In determining the appropriate scope of the revenue base for federal universal service support, the

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[2064] *See supra* section X.F.2.

[2065] PageMart comments at 7-8. *See also* Arch comments at 3-6; Celpage comments at 9-10; PageNet comments at 10-13; PNPA comments at 3-5; AirTouch reply comments at 25; Centennial reply comments at 3-4 (claiming unless its CMRS is a substitute for land line service, CMRS operator should make reduced contribution).

Joint Board Recommended Decision stressed that the 1996 Act "reflects the continued partnership among the states and the Commission in preserving and advancing universal service."[2066] Ultimately, the Recommended Decision concluded that the "role of complementary state and federal universal service mechanisms require[d] further reflection" before the Joint Board could make a recommendation as to whether the revenue base for the federal universal support mechanisms for the high cost and low-income assistance programs should be based on intrastate as well as interstate revenues.[2067] Nonetheless, the Joint Board was able to recommend that "universal support mechanisms for schools and libraries and rural health care providers be funded by assessing both the intrastate and interstate revenues of providers of interstate telecommunications services."[2068]

807. Although we conclude that section 254 grants the Commission the authority to assess contributions for the universal service support mechanisms for rural, insular, and high cost areas and low income consumers from intrastate as well as interstate revenues and to require carriers to seek authority from states to recover a portion of the contribution in intrastate rates, we decline to exercise the full extent of our authority. The decision to decline to exercise the entirety of our authority is intended to promote comity between the federal and state governments and is based on our respect for the states' historical expertise in providing for universal service.

[2066] Recommended Decision, 12 FCC Rcd at 500.

[2067] Recommended Decision, 12 FCC Rcd at 501.

[2068] Recommended Decision, 12 FCC Rcd at 499.

808. There are three dimensions to determining how the recovery component of the federal universal service mechanisms will work. The first dimension is determining the total amount of support required to meet the federal obligation imposed by section 254. This issue is addressed elsewhere in this Order, specifically in section IV where we determine which services we will support and in sections VII and VIII where we determine the appropriate amount of support for the high cost and low-income support mechanisms and sections X and XI, where we determine the appropriate amount of support for schools, libraries, and rural health care providers. The second dimension to our inquiry is whether we should assess carriers' contributions to the universal service support mechanisms from interstate revenues only or from interstate and intrastate revenues. As to the second dimension, we adopt the Joint Board's recommendation "that universal service support mechanisms for schools and libraries and rural health care providers be funded by assessing both the intrastate and interstate revenues of providers of interstate telecommunications services."[2069] The Joint Board determined that it was premature for it to recommend that we assess carriers' contributions for the high cost and low-income support mechanisms based on carriers' intrastate as well as interstate revenues. We have decided to continue to assess carriers' contributions for the high cost and low-income support mechanisms based only upon the carriers' interstate revenues because we want to continue to work with the Joint Board on this issue to develop a unified approach to the low-income

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[2069] Recommended Decision, 12 FCC Rcd at 499.

and high cost mechanisms and because we believe that in the meantime the states will continue to provide for the high cost and low-income mechanisms in such a manner that the mechanisms will be sufficiently funded.

809. The third dimension to our inquiry is whether carriers may recover their contributions to the universal service support mechanisms through rates for interstate services or through a combination of rates for interstate and rates for intrastate services. The Joint Board did not address this question. Because the Joint Board did not recommend that we authorize carriers to recover their contributions via rates for intrastate services, we conclude that at least for the present we should maintain our traditional method of providing for recovery, which permits carriers to recover their federal universal service contributions through rates for interstate services only. As described below, we believe that this approach will best promote the continued affordability of basic residential service. For the same reason, i.e., to maintain and promote the affordability of basic residential service, we also are declining to create a single interstate fee that would be paid by basic residential dialtone subscribers. We will, however, continue to seek guidance from the Joint Board as to whether carriers should be required to seek state authorization to recover a portion of the universal service contribution in intrastate rates, rather than in interstate rates alone.

2. Background

810. The Joint Board recommended that support for eligible schools, libraries, and rural health care providers

be based on revenues derived from interstate and intrastate telecommunications services but did not issue a recommendation regarding the revenue funding base for support for high cost areas or low-income consumers.[2070]

811. As detailed in Appendix J containing the comment summaries, the commenters generally disagreed as to whether intrastate telecommunications revenues should be included when assessing carrier contributions to the support mechanisms and as to whether the Commission has the statutory authority to include those revenues.

812. On April 24, 1997, a majority of the state members of the Joint Board filed a report with the Commission discussing their recommendations on the funding of the universal service support mechanisms.[2071] The majority state members of the Joint Board recommended that all of the universal service mechanisms be supported "through an assessment on the interstate and intrastate revenues of interstate telecommunications carriers."[2072] The majority

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[2070] Recommended Decision, 12 FCC Rcd at 499. Two of the state members of the Joint Board, Commissioner McClure and Commissioner Schoenfelder, dissented from that portion of the Recommended Decision that recommended that the support mechanisms for eligible schools, libraries, and rural health care providers be based on revenues derived from intrastate as well as interstate revenues. Recommended Decision, 12 FCC Rcd at 571, 576.

[2071] Majority Opinion of the State Members of the Joint Board on the Funding of Universal Service, dated Apr. 24, 1997 ("Majority State Members' Jurisdiction Report").

[2072] Majority State Members' Jurisdiction Report at 1.

state members also concluded, however, that if implementation of the modified high cost support mechanisms "must await further refinement" of a forward-looking cost methodology, then they would "support an interim policy of assessing only interstate revenues."[2073] Commissioners McClure and Schoenfelder dissented from the majority state members' conclusion that the Commission should assess contributions for the support mechanisms from intrastate as well as interstate revenues.[2074]

3. Discussion

a. General Jurisdiction Over Universal Service Support Mechanisms

813. For the reasons described below, we conclude that the Commission has jurisdiction to assess contributions for the universal service support mechanisms from intrastate as well as interstate revenues and to require carriers to seek state (and not federal) authority to recover a portion of the contribution in intrastate rates. Although we expressly decline to exercise the entirety of this jurisdiction, we believe it is important to set forth the contours of our authority in this Order.

814. Our authority over the universal service support mechanisms is derived first and foremost from the plain language of section 254. First, section 254(a) provides that rules "to implement" the section are to be

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[2073] Majority State Members' Jurisdiction Report at 2.

[2074] Dissenting Statement of Commissioner Kenneth McClure and Commissioner Laska Schoenfelder, filed Apr. 23, 1997 ("McClure/Schoenfelder Dissent").

recommended by the Joint Board, and those recommendations, in turn, are to be implemented by the Commission.[2075] Thus, the Commission has the ultimate responsibility to effectuate section 254. Further, Congress reemphasized the Commission's authority independent of the Joint Board by directing in section 254(c)(2) that the concept of universal service is an "evolving level of telecommunications *that the Commission shall establish* periodically."[2076] Thus, Congress expressly authorized the Commission to define the parameters of universal service.[2077]

815. Section 254(d) also mandates that interstate telecommunications carriers "shall contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and *sufficient* mechanisms established by the Commission to preserve and advance universal service."[2078] In thus prescribing that the support

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[2075] 47 U.S.C. § 254(a)(2).

[2076] 47 U.S.C. § 254(c)(1) (emphasis added).

[2077] Congress expressly directed the Commission to initiate a proceeding to implement Section 254. 47 U.S.C. § 254(a)(1). Thus, there can be no doubt that Congress intended the Commission to promulgate regulations to effectuate section 254. *See* 47 U.S.C. § 254(a)(1)&(2). Of course, the Commission also possesses "expansive" rulemaking authority over all provisions of the Communications Act, and in particular over the provisions of Title II of the Communications Act, of which Section 254 is a part. *See* 47 U.S.C. §§ 154(i), 21(b), 303(r); *NBC v. United States*, 319 U.S. 190, 219 (1943).

[2078] 47 U.S.C. § 254(d) (emphasis added). *See also* 47 U.S.C. § 254(b)(5) ("There should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service.")

mechanisms be "sufficient," Congress obligated the Commission to ensure that the support mechanisms satisfy section 254's goal of "preserving and advancing universal service," consistent with the principles set forth in section 254(b), including the principle that quality services should be available at "just, reasonable, and affordable rates."[2079] In so doing, Congress expressly granted the Commission jurisdiction to establish support mechanisms of a sufficient size adequately to support universal service.

816. In essence, the provisions of section 254 direct that the Commission ultimately prescribe what services should be supported, and they mandate that the Commission ensure that the support for those services is "specific, predictable, and sufficient."[2080] Although the states are independently obligated to ensure that support mechanisms are "specific, predictable, and sufficient" and that rates are "just, reasonable, and affordable,"[2081] there is no doubt that the Commission – with the help of the states – is to establish in the first instance what services should be supported and what are the necessary mechanisms to do so. This is because the states' authority to adopt sufficient support mechanisms is restricted to only those mechanisms that are consistent with and do not burden the federal mechanisms.[2082] Because state universal service

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[2079] 47 U.S.C. § 254(b)(1); 47 U.S.C. § 254(i) ("The Commission and the States should ensure that universal service is available at rates that are just, reasonable, and affordable.").

[2080] 47 U.S.C. § 254(d); *see also* 47 U.S.C. § 254(b)(5).

[2081] 47 U.S.C. §§ 254(b)(5), (d), (i).

[2082] 47 U.S.C. § 254(f).

mechanisms must be consistent and must not conflict with the federal mechanisms, it is reasonable to conclude that section 254 grants the Commission the primary responsibility and authority to ensure that universal service mechanisms are "specific, predictable, and sufficient" to meet the statutory principle of "just, reasonable, and affordable rates."[2083] The fact that the Commission has this authority does not preclude the Commission from continuing to work with the states to provide for universal service, so long as this partnership results in support mechanisms that comply with the mandates of section 254.

817. Congress recognized that the services supported by the universal service support mechanisms would include both intrastate and interstate services. For example, in section 254(b)(3), Congress established the principle that the Commission is to formulate its universal service rules and policies so that "[c]onsumers in all regions of the Nation . . . have access to telecommunications and information services, including interexchange services."[2084] The fact that universal service *includes* access to interexchange services, the traditional focus of federal telecommunications law, shows that universal service includes *more* than access to interexchange services. Indeed, the traditional core goal of universal service has been to ensure that basic residential telephone service, which is primarily an intrastate service, is affordable. The goal of keeping basic residential rates low traditionally

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[2083] 47 U.S.C. § 254(b)(1) & (5), (d), (i).

[2084] 47 U.S.C. § 254(b)(3).

has been advanced by both the FCC and the state commissions, which have kept intrastate residential rates low by means of implicit support mechanisms such as allowing LECs to raise rates on business lines and on vertical services such as call waiting to levels greater than those that would be charges in a competitive market. In section 254(b), Congress made affordable basic service a goal of federal universal service, by that determination, Congress meant that both interstate and intrastate services should be affordable.[2085] The Joint Board agreed with this conclusion by including intrastate services on the list of telecommunications services that it recommended for universal service support pursuant to section 254(c). Congress also directed the Commission and the states to strive to make implicit support mechanisms explicit. We have found nothing in the statute or legislative history to show that, notwithstanding Congress's mandate to make universal service subsidies explicit, Congress intended to alter the current arrangement by requiring interstate services to assume the entire burden of providing for universal service. Accordingly, the section 254 mandate covers both interstate and intrastate services and therefore it is also reasonable that the Commission, in ensuring that the overall amount of the universal support mechanisms is "specific, predictable, and sufficient," may also mandate that contributions be based on carriers' provision of intrastate services. As discussed below, however, we decline to exercise the full extent of this authority out of respect

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[2085] As discussed below, we are accomplishing the goal of affordable service for eligible schools, libraries, and rural health care providers by assessing contributions based on both interstate and intrastate revenues.

for the states and the Joint Board's expertise in protecting universal service.

818. We fully appreciate and support the continuation of the historical informal partnership between the states and the Commission in preserving and advancing the universal service support mechanisms envisioned by section 254. Indeed, we believe that section 254 envisions the continuation of this partnership. We conclude nonetheless that this partnership does not affect the Commission's jurisdiction to assess contributions sufficient to meet that need from both interstate and intrastate revenues. Indeed, in recommending that we assess contributions based on intrastate and interstate revenues, the Majority State Members' Jurisdiction Report recognized that section 254 "represents a significant departure from the current method of funding existing universal service mechanisms," but that there still is a "need for federal and state regulators to manage the transition to competitive markets together."[2086] We have concluded that we will assess contributions for the support mechanisms for eligible schools, libraries, and rural health care providers from intrastate and interstate revenues. We also conclude that, when we assess contributions based on intrastate as well as interstate revenues, we have the authority to refer carriers to the states to seek authority to recover a portion of their intrastate contribution from intrastate rates. We have not adopted this approach in this Order. In section 254(f) Congress expressly allowed only for those state universal service mechanisms that are not "inconsistent with the Commission's rules to preserve and advance

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[2086] Majority State Members' Jurisdiction Report at 2.

universal service."[2087] Thus, the statutory scheme of section 254 demonstrates that the Commission ultimately is responsible for ensuring sufficient support mechanisms, that the states are encouraged to become partners with the Commission in ensuring sufficient support mechanisms, and that the states may prescribe additional, supplemental mechanisms.[2088] Section 254 also *permits* the Commission to coordinate with the states in establishing the universal service support mechanisms so long as this cooperative relationship produces universal service support mechanisms that comply with the mandates of section 254 and we have adopted this approach with respect to the high cost and low-income support mechanisms.

819. There is no indication that Congress's authorization in section 254(f) of a separate support mechanism covering intrastate carriers evidences an intent that the amount of a carrier's contributions to the respective support mechanisms similarly should be based on the type of

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[2087] 47 U.S.C. § 254(f); *see also* 47 U.S.C. § 254(b)(5).

[2088] *Compare* 47 U.S.C. § 254(b) ("The Joint Board and the Commission shall base policies for the preservation and advancement of universal service on the following principles . . . "); § 254(c)(1) ("Universal service is an evolving level of telecommunications services that the Commission shall establish") *with* 47 U.S.C. § 254(f) ("A State may adopt regulations *not inconsistent* with the Commission's rules to preserve and advance universal service. . . . A State may adopt regulations to provide for *additional* definitions and standards to preserve and advance universal service within that State only to the extent that such regulations adopt *additional* specific, predictable, and sufficient mechanisms to support such definitions or standards and *do not rely on or burden* Federal universal service support mechanisms") (emphasis added).

communications service, interstate or intrastate, provided by the carrier. Nothing in the legislative history supports such an inference. Indeed, the legislative history indicates that states may continue to have jurisdiction over implementing universal service mechanisms for intrastate services supplemental to the federal mechanisms so long as "the level of universal service provided by each state meets the minimum definition of universal service established [under section 254] and a State does not take any action inconsistent with the obligation for all telecommunications carriers to contribute to the preservation and advancement of universal service" established under section 254.[2089]

820. Several state PUCs assert that the Commission does not have jurisdiction over interstate and intrastate telecommunications revenues because such a scheme would potentially subject carriers' intrastate revenues to two support mechanisms, one federal and one state.[2090] The commenters argue that this double burden will hinder states' abilities to address state universal service issues. It is not clear to us how states would be hindered, because many of the carriers contributing to state and federal support mechanisms also would be eligible to receive both state and federal support. In any event, the statutory language envisions that both the federal and state support mechanisms will support basic intrastate

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[2089] Joint Explanatory Statement at 128.

[2090] *See e.g.*, Alabama PSC comments at 2-3; Kansas CC comments at 6; Kentucky PSC comments at 2-3.

and interstate services and, moreover, the statutory language plainly envisions that the state mechanisms will be in addition to the federal mechanisms.[2091]

821. Section 2(b) of the Communications Act is not implicated in this jurisdictional analysis. Section 2(b) provides that "nothing in [the Communications Act] shall be construed to apply or give the Commission jurisdiction with respect to . . . charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communications service by wire or radio."[2092] Even when the Commission exercises jurisdiction to assess contributions for universal service support from intrastate as well interstate revenues (i.e., for eligible schools and libraries and rural health care providers), such an approach does not constitute rate regulation of those services or regulation of those services so as to violate section 254(b). Instead, the Commission merely is supporting those services, as expressly required by Congress in section 254 and as recommended by the Joint Board. Indeed, as discussed above, Congress expressly mandated that the Commission ensure that such support mechanisms be sufficient. As recognized by several of the commenters, when assessing contributions based on intrastate and interstate revenues, the Commission merely is calculating a federal charge based on both interstate and intrastate revenues, which is distinct from regulating the rates and conditions of interstate service.[2093]

[2091] 47 U.S.C. § 254(f).

[2092] 47 U.S.C. § 152(b).

[2093] *See, e.g.*, Roseville Tel. Co. comments at 5; Vermont PSB comments at 5.

822. Moreover, although the Commission is not adopting this approach, section 2(b) would not be implicated even if the Commission were to refer carriers to the states to obtain authorization to recover their intrastate contributions via intrastate rates, which it is not doing, because the Commission would still be referring the matter to the states' authority over changes in intrastate rates and the Commission itself would not be regulating those rates. In any event, to the extent that section 2(b) would be implicated in either of these approaches (assessment or recovery), section 254's express directive that universal service support mechanisms be "sufficient" ameliorates any section 2(b) concerns because, as a rule of construction section 2(b) only is implicated where the statutory provision is ambiguous.[2094] Here, as discussed above, section 254 is unambiguous in that the services to be supported have intrastate as well as interstate characteristics and in that the Commission is to promulgate regulations implementing federal support mechanisms covering the intrastate and interstate characteristics of

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[2094] Section 601 also is consistent with our conclusion. Section 601 of the 1996 Act provides that the Act and its amendments "shall not be construed to modify, impair, or supersede Federal, State, or local law unless expressly so provided in such Act or amendments." 47 U.S.C. § 601. We are not modifying any state law, but merely implementing a federal mandate and merely continuing the federal-state partnership that historically has provided for universal service. Section 261 also is consistent with our analysis because we are in no way preventing the states from continuing or implementing universal service mechanisms so long as those mechanisms are consistent with our mechanisms. 47 U.S.C. § 261.

the supported services. Therefore, the unambiguous language of section 254 overrides section 254(b)'s otherwise-applicable rule of construction.

823. Further, to the extent that commenters assert that the Communications Act generally divides the world into two spheres – Commission jurisdiction over interstate carriers and interstate revenues and state jurisdiction over intrastate carriers and intrastate revenues – section 254 blurs any perceived bright line between interstate and intrastate matters. The services that will be supported pursuant to this Order include both intrastate and interstate services. As discussed above, although section 254 anticipates a federal-state universal service partnership, section 254 grants the Commission primary responsibility for defining the parameters of universal service. Indeed, the recognition of this fact presumably led Congress to require Joint Board involvement in that Congress recognized that it was important for the Commission to consider the states' recommendations because the regulations ultimately adopted inevitably would affect the states' traditional universal service programs.[2095] The new requirements in the statute to consider the needs of schools, libraries, and health care providers in and of themselves require a fresh look at universal service. The legislative history also indicates that the Commission, in consultation with the Joint Board, was not to be bound by mechanisms used currently. For example, the Joint Explanatory Statement

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[2095] It would be anomalous for Congress to have required such an active role for the states in a process concerned only with interstate matters.

warned against reliance on some current methodologies by stating that any support mechanisms should be "explicit, rather than implicit as many support mechanisms are today."[2096] Similarly, the Senate Report on § 254 states that "the bill does not presume that any particular existing mechanism for universal service support must be maintained or discontinued."[2097] Therefore, we conclude that section 254 grants us the authority to assess contributions for the universal service support mechanisms from intrastate as well as interstate revenues and to refer carriers to seek state (and not federal) authorization to recover a portion of the contribution in intrastate rates. As described below, however, we see no need at this time to exercise the full extent of our jurisdiction.

b. Scope of the Revenue Base for the High Cost and Low-Income Support Mechanisms

824. We have determined that we will assess and permit recovery of contributions to the rural, insular, and high cost and low-income support mechanisms based only on interstate revenues. We will seek further guidance on this subject from the Joint Board because the Joint Board did not at the time of the Recommended Decision make a recommendation as to whether the revenue base for the high cost and low-income mechanisms should include intrastate as well as interstate revenues. We believe that our approach to assessment and recovery

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[2096] Joint Explanatory Statement at 131. As previously noted, many of the implicit support mechanisms today are intrastate.

[2097] S. Rep. No. 23, 104th Cong., 1st Sess. 25 (1995).

serves the public interest because it promotes comity between the federal and state governments and because it continues the traditional informal partnership between the federal government and the states in supporting universal service. Moreover, as described below, we believe that our approach for permitting recovery of carriers' contributions will help ensure the continued affordability of basic residential dialtone service. We fully anticipate that each of the states will join with us in ensuring the establishment of "specific, predictable, and sufficient" universal service support mechanisms.[2098]

825. *Recovery of Carriers' Contributions to the High Cost and Low-Income Support Mechanisms.* We have determined to continue our historical approach to recovery of universal service support mechanisms, that is, to permit carriers to recover contributions to universal service support mechanisms through rates for interstate services only. In discussing recovery we are referring to the process by which carriers' recoup the amount of their contributions to universal service. Although the Joint Board did not address this issue, as discussed below, the Joint Board concluded that the "role of complementary state and federal universal service mechanisms require[d] further reflection" before the Joint Board could recommend that we assess contributions based on intrastate as well as interstate revenues.[2099] Therefore, we believe that our decision to provide for recovery based only on rates for interstate services is not inconsistent with the Joint Board Recommended Decision.

[2098] 47 U.S.C. § 254(b)(5), (d).

[2099] Recommended Decision, 12 FCC Rcd at 501.

826. We believe that our approach to recovery promotes comity between the federal and state governments in that our approach will help us to develop a unified federal-state approach to universal service. As discussed above in section XIII.E.3.a, section 254 permits, but does not require, the Commission to assess contributions based only on interstate revenues (instead of on interstate and intrastate revenues). While the Joint Board further considers these jurisdictional issues, we deem it to be in the public interest to maintain the current relationship whereby the federal government oversees the assessments and recovery of the interstate share of the necessary contributions, and the state governments assess and provide recovery for the intrastate share of the necessary contributions. We also deem it in the public interest to maintain the traditional federal-state partnership because many states are in the process of altering their own universal service programs to comply with section 254 and we prefer to await the outcome of these reforms (which are expected later this year) before altering the federal-state relationship that thus far has provided for universal service for high cost areas and low-income consumers. Thus, we see no need for an immediate change in the manner in which these intrastate contributions are assessed and recovered.

827. Our decision as to the recovery of universal service contributions also is consistent with the statutory principle of providing affordable basic residential service in that by providing for recovery through interstate

mechanisms we are avoiding a blanket increase in charges for basic residential dialtone service.[2100]

828. By providing for recovery of contributions to support universal service in rural, insular, and high cost areas and for low-income consumers solely from rates for interstate services, we also avoid any of the asserted difficulties raised by commenters such as NYNEX that oppose assessing contributions from interstate and intrastate revenues because some carriers may face difficulty recovering contributions based on intrastate revenues.[2101] Similarly, to the extent that some commenters were concerned that section 254(b) prevents us from providing for recovery via rates for intrastate services, there are no such problems – perceived or otherwise – with our decision to provide for recovery solely through rates for interstate services.

829. Under our recovery mechanism, carriers will be permitted, but not required, to pass through their contributions to their interstate access and interexchange customers.[2102] We note that, if some carriers (e.g., IXCs) decide to recover their contribution costs from their customers, the carriers may not shift more than an equitable share of their contributions to any customer or group of customers.[2103] As discussed below in section XIII.F, we

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[2100] 47 U.S.C. § 254(b)(1).

[2101] NYNEX comments at 25. *See also* Ohio PUC reply comments at 17-18.

[2102] The details of the recovery mechanism for price cap LECs are explained in our companion *Access Charge Reform Order*, section VI.D.2.b.

[2103] In the *Local Competition Order*, the Commission stated that wholesale rates should be based on retail prices less

also have determined that the interstate contributions will constitute the substantial cause that would provide a public interest justification for filing federal tariff changes or making contract adjustments.

830. We have determined that ILECs subject to our price cap rules may treat their contributions for the new universal service support mechanisms as an exogenous cost change. We outline the precise contours of the exogenous change available to federal price cap carriers in our *Access Charge Reform Order*, adopted contemporaneously with this Order. For carriers not subject to federal price caps (e.g., other ILECs), we have determined to permit recovery of universal service contributions by applying a factor to increase their carrier common line charge revenue requirement. Of course, LECs and their affiliates that provide interLATA interstate services each will have their own universal service obligations and, therefore, the affiliates will be required to recover their own universal service contributions.[2104]

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avoided costs. *See Local Competition Order*, 11 FCC Rcd 15,954-15,957. We note that universal service contributions should be an additional avoided cost taken into account by states when setting the avoided cost discount rate. That is, avoided costs should include the contribution that an ILEC avoids from providing service to a reseller as opposed to an end user.

[2104] Section 272 of the 1996 Act provides that BOCs must provide in region interLATA services through a separate affiliate. 47 U.S.C. § 272(a). Previously, in the Competitive Carrier Fifth Report and Order, 98 FCC 2d 1191, 1198-99 n. 23 (1984), the Commission held that LECs must provide certain interstate services via affiliates or else be treated as a dominant carrier. The Commission recently reaffirmed this requirement.

831. *Assessment of the Revenue Base for the High Cost and Low-Income Support Mechanisms.* In addition to the recovery mechanisms discussed above, we also consider whether we should assess contributions to the universal service support mechanisms based solely on interstate revenues or on both interstate and intrastate revenues. To promote comity between the federal and state governments, we have decided to follow our approach to the recovery issues and thus to assess contributions for the high cost and low income support mechanisms based solely on interstate revenues. We have every reason to believe that the states will continue to participate fully in this federal-state partnership and that the contributions collected by both jurisdictions will be sufficient. As discussed above, we conclude that our assessment approach also is warranted because the states presently are reforming their own universal service programs.

832. The approach we adopt today is consistent with the approach taken by the Joint Board. Specifically, the Joint Board concluded that the "decision as to whether intrastate revenues should be used to support the high cost and low income assistance programs should be coordinated with the establishment of the scope and magnitude of the proxy-based fund, as well as with state universal service support mechanisms."[2105] Although the

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Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area and Policy and Rules Concerning the Interstate, Interexchange Marketplace, *Second Report and Order in CC Docket No. 96-149 and Third Report and Order in CC Docket No. 96-61*, CC Docket Nos. 96-149, 96-61, FCC 97-142 (rel. Apr. 18, 1997).

[2105] Recommended Decision, 12 FCC Rcd at 499.

Joint Board may have anticipated that these decisions all would be made in this Order, the crux of the Joint Board's analysis is that the question of interstate/intrastate contribution should be coordinated with the issues of appropriate forward-looking mechanisms and appropriate revenue benchmarks.[2106] Because those issues will be resolved in the future, we believe it would be premature for us to assess contributions on intrastate as well as interstate revenues. Our approach also is consistent with the recent recommendations contained in the Majority State Members' Jurisdiction Report. That report recommended that the Commission assess contributions for all support mechanisms from intrastate and interstate revenues, but supported the Commission's present approach to assess only interstate revenues for the high cost mechanisms until a forward-looking cost methodology is developed.[2107] Given that two state members of the Joint Board dissented from the recommendation that we assess both interstate and intrastate revenues, we believe that it is in the public interest to proceed to assess only interstate revenues while a unified federal-state approach is developed for the high cost and low-income support mechanisms.

833. Our assessment procedure is as follows. Between January 1, 1998 and January 1, 1999, contributions for the existing high cost support mechanisms and low-income support programs will be assessed against interstate end-user telecommunications revenues.[2108]

[2106] Recommended Decision, 12 FCC Rcd at 501.

[2107] Majority State Members' Jurisdiction Report at 2.

[2108] *See infra* section XIII.F for a discussion of the end-user telecommunications revenues method of assessing

Beginning on January 1, 1999, the Commission will modify universal service assessments to fund 25 percent of the difference between cost of service defined by the applicable forward-looking economic cost method less the national benchmark, through a percentage contribution on interstate end-user telecommunications revenues. We have decided to institute this approach to assessment on January 1, 1999 to coordinate it with the shift of universal service support for rural, insular, and high cost areas served by large LECs from the access charge regime to the section 254 universal service mechanisms.

834. Our decision to provide 25 percent of the necessary support for high cost providers is consistent with Congress's mandate that universal service support "should be explicit."[2109] As explained in the Joint Explanatory Statement, Congress intended that, to the extent possible, "any support mechanisms continued or created under new section 254 should be explicit, rather than implicit as many support mechanisms are today."[2110] Beginning on January 1, 1999, we will convert the existing implicit support to an explicit 25 percent support. We do not, however, attempt to identify existing state-determined intrastate implicit universal service support presently effected through intrastate rates or other intrastate

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contributions. Following January 1, 1998, the new funding mechanism for high cost and low-income programs will supersede the current funding mechanism for those programs.

[2109] 47 U.S.C. 254(e).

[2110] Joint Explanatory Statement at 131.

rules, nor do we attempt to convert such implicit intrastate support into explicit federal universal service support. Indeed, as discussed above, we have decided to respect the states' historical role and expertise in providing the additional, necessary amount of support and we leave it to the states to convert their own programs into explicit support mechanisms. As states do so, we will be able to assess whether additional federal universal service support is necessary to ensure that quality services remain "available at just, reasonable and affordable rates."[2111] For our programs for low-income consumers, established under the jurisdiction of sections 1, 4(i), and 201-205, we adopt an approach consistent with our historical support for Lifeline/LinkUp programs and provide support for Lifeline/LinkUp from state and federal sources. Therefore, we provide $3.50 in federal support for every Lifeline consumer, which will be for ILECs a waiver of the SLC, plus an additional $1.75 pending state commission approval of a reduction in state rates. In addition, assuming state commission approval of state rate reductions, we will provide $1.00 of support for every $2.00 of support provided by the states, up to a maximum of $7.00 of federal support.

835. We are aware that some commenters are concerned that our assessment approach may have certain administrative problems in that carriers may have an incentive to classify revenues as intrastate rather than interstate to avoid collection. We also are aware that the Joint Board did not want service providers to make business decisions based on their obligations to contribute to

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[2111] 47 U.S.C. 254(b)(1).

federal support mechanisms.[2112] We share these concerns and we hope that the states will work with us to address them. Specifically, we hope to minimize any administrative problems by encouraging a federal-state partnership whereby together the Commission and the states will assess the entirety of the support mechanisms (25 percent from federal and 75 percent from state mechanisms). We are however aware of the need to monitor the administration of the support mechanisms and we will monitor the collection and distribution processes to ensure that they do not produce inequitable results. We expect that the states and the Joint Board will do the same.

836. In response to COMSAT's comments, we clarify that carriers that provide interstate services must include all revenues derived from interstate and international telecommunications services. Thus, international telecommunications services billed to a domestic end user will be included in the contribution base of a carrier that provides interstate telecommunications services.[2113] Section 2(b) of the Act grants states the authority to regulate intrastate rates, but in contrast section 2(a) grants the Commission sole jurisdiction over interstate and foreign communications.[2114] Foreign communications are defined as a "communication or transmission from or to any place in the United States to or from a foreign country, or between a station in the United States and a

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[2112] Recommended Decision, 12 FCC Rcd at 481-482.

[2113] Providers of interstate telecommunications required to contribute would include the revenues from international telecommunications billed to domestic end users.

[2114] 47 U.S.C. § 152(a) & (b).

mobile station located outside of the United States."[2115] We find that it would serve the public interest to require carriers providing interstate telecommunications services to base their contributions on revenues derived from their interstate and foreign or international telecommunications services. Contributors that provide international telecommunications services benefit from universal service because they must either terminate or originate telecommunications on the domestic PSTN. Therefore, we find that contributors that provide international telecommunications services should contribute to universal service on the basis of revenues derived from international communication services, although, as discussed above, revenues from communications between two international points would not be included in the revenue base.

c. Scope of the Revenue Base for the Support Mechanisms for Eligible Schools, Libraries, and Rural Health Care Providers

837. We adopt the Joint Board's recommendation that "universal support mechanisms for schools and libraries and rural health care providers be funded by contributions based on both the intrastate and interstate revenues of providers of interstate telecommunications services."[2116] We adopt this approach not only because the Joint Board recommended it, but also because the

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[2115] 47 U.S.C. § 153(17).

[2116] Recommended Decision, 12 FCC Rcd at 499.

eligible schools, libraries, and rural health care mechanisms are new, unique support mechanisms that have not historically been supported through a universal service funding mechanism. Nonetheless, for now, we will provide for recovery of the entirety of these contributions via interstate mechanisms.

838. As with recovery of the amounts carriers contribute to the high cost and low-income support mechanisms, we have decided to permit recovery of contributions for the support mechanisms for eligible schools, libraries, and rural health care providers solely via rates for interstate services. Indeed, our rationale is even more compelling for the support mechanisms for eligible schools, libraries, and rural health care providers because those mechanisms will be supported based upon both intrastate and interstate revenues and, therefore, there is a heightened concern that carriers would recover the portion of their intrastate contributions attributable to intrastate services through increases in rates for basic residential dialtone service, contrary to the affordability principle contained in section 254(b)(1). Therefore, carriers may recover these contributions solely through rates for interstate services, in the same manner that they will recover their contributions to the high cost and low-income support mechanisms, as described above.

839. We find that our approach also minimizes any perceived jurisdictional difficulties under section 2(b) because we do not require carriers to seek state authorization to recover the contributions attributable to intrastate revenues. Nonetheless, carriers with interstate revenues far less than their intrastate revenues assert that

they will be required to recover unfairly large contributions from their interstate customers and that this outcome is inequitable.[2117] These carriers misinterpret the statute's direction that contributions be "equitable and non-discriminatory."[2118] "Equitable" does not mean "equal."[2119] In the past, telecommunications subsidies have been raised by assessing greater amounts from services other than basic residential dialtone services. Competition in the telecommunications marketplace, however, should drive prices for services closer to cost and eliminate the viability of shifting costs from residential to business or from basic local service to long distance. Congress did direct that contributions be non-discriminatory. This we accomplish by making the formula for calculating contributions the same for all competitors competing in the same market segment. Although a provider of business services may pay a greater contribution than a provider of residential service, the provider of business services pays contribution according to the same formula as other providers of business services. Similarly, simply because a provider has far more interstate than intrastate revenue does not make a formula based on interstate revenue discriminatory, provided the formula

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[2117] Sprint comments at 7-9.

[2118] 47 U.S.C. § 254(b)(4).

[2119] Courts have recognized the "importance of treating parties alike when they participate in the same event or when the agency vacillates *without reason* in its application of a statute or the implementing regulations." *New Orleans Channel 20, Inc. v. FCC*, 830 F.2d 361, 366 (D.C. Cir. 1987) (emphasis added); *Melody Music, Inc. v. FCC*, 345 F.2d 730 (D.C. Cir. 1965).

is the same for other providers of similar interstate services.

840. As to the assessment of contributions for the support mechanisms for eligible schools, libraries, and rural health care providers, the Commission is adopting the Joint Board's recommendation that these contributions be based upon both interstate and intrastate revenues.[2120] We have selected this approach because these are new and unique federal programs and states have not supported these initiatives to the same extent that they have supported other universal service support mechanisms. In contrast to the high cost mechanisms, many states do not already have programs in place that would guarantee sufficient support mechanisms for eligible schools, libraries, and rural health care providers. Therefore, we are not as confident that a federal-state partnership would sufficiently support these new and unique support mechanisms, particularly in the early years of the

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[2120] Our approach also is consistent with the recent Majority State Members' Jurisdiction Report, which reiterated the Joint Board's recommendation that the Commission should assess contributions for the support mechanisms for eligible schools, libraries, and rural health care providers from interstate and intrastate revenues. Majority State Members' Jurisdiction Report at 2. Although two state members of the Joint Board dissented from this recommendation, *see* McClure/Schoenfelder Dissent, in contrast to the high cost and low-income support mechanisms where we are attempting to develop a unified approach, we conclude that notwithstanding this dissent it is important for the Commission to assess both interstate and intrastate revenues for the other support mechanisms because there are not in place sufficient state mechanisms to ensure that section 254's mandates are satisfied.

program. Because section 254 obligates the Commission to ensure the sufficiency of this support program, we deem it necessary to adopt an approach that will guarantee that this statutory mandate is satisfied. In addition, assessing both intrastate and interstate revenues to fund the support mechanisms for eligible schools, libraries, and rural health care providers is more feasible than for the other mechanisms because the amount of the new support mechanisms will be smaller than the other mechanisms (i.e., the combined amounts of the federal and state high cost and low-income support mechanisms will be greater than the total amount of the schools, libraries, and rural health care mechanisms). Therefore, we believe that it is appropriate for us to assess a contributor based upon its intrastate and interstate revenues for the schools, libraries, and rural health care support mechanisms.

841. For the same reasons described above, we conclude that carriers that provide interstate services must include all revenues derived from interstate and international telecommunications services. Contributors that provide international telecommunications services benefit from universal service because they must either terminate or originate telecommunications on the domestic PSTN. Therefore, we find that contributors that provide international telecommunications services should contribute to universal service on the basis of revenues derived from those services.

F. Basis for Assessing Contributions

1. Background

842. Section 254(d) states that "[e]very telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service."[2121] In the NPRM, the Commission suggested three different bases for calculating contributions to the universal service mechanisms established by the Commission: gross revenues; gross revenues net of payments to other carriers for telecommunications services (net telecommunications revenues); and per-line or per-minute charges.[2122] The Commission invited comment on the relative merits of these methods and the extent to which they satisfy the requirements of the Act.[2123] The Commission also sought comment on any other alternative methodologies for calculating a carrier's or service provider's contribution to universal service support. The Commission instructed commenters to address which method would be the most easily administered and competitively neutral, taking into account the possibility that the Commission could require non-carrier providers of telecommunications services to contribute.[2124] The Joint Board recommended that contributions be based on gross revenues derived from

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[2121] 47 U.S.C. § 254(d). *See also* 47 U.S.C. § 254(b)(4).

[2122] NPRM at paras. 122-125.

[2123] NPRM at para. 125.

[2124] NPRM at paras. 122-126.

telecommunications services net of payments to other carriers for telecommunications services because that method would eliminate the double payment problem,[2125] would assess contributions on a value-added basis, and is familiar to the Commission and the industry.[2126]

2. Discussion

843. We agree with the Joint Board's recommendation that we must assess contributions in a manner that eliminates the double payment problem, is competitively neutral and is easy to administer.[2127] To address the Joint Board's concerns, we find that contributions should be based on end-user telecommunications revenues. Based on new information in the record, we find that this basis for assessing contributions represents a basis for our universal service support mechanisms more administratively efficient than the net telecommunications revenues method recommended by the Joint Board while still advancing the goals embraced by the Joint Board. We note that we will assess contributions, i.e., raise sufficient funds to cover universal service's funding needs, only after we have determined the total size of the support mechanisms.

844. We will assess contributions based on telecommunications revenues derived from end users for several

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[2125] *See* section XIII.F.2, *infra* for a description of the double payment problem.

[2126] Recommended Decision, 12 FCC Rcd at 495.

[2127] Recommended Decision, 12 FCC Rcd at 495.

reasons, including administrative ease and competitive neutrality. The net telecommunications revenues and end-user telecommunications revenues methods are relatively equivalent because they assess contributions based on substantially similar pools of revenues.[2128] Therefore, we conclude that contributions will be based on revenues derived from end users for telecommunications and telecommunications services, or "retail revenues." Unlike retail revenues, however, end-user telecommunications revenues include revenues derived from SLCs. End-user revenues would also include revenues derived from other carriers when such carriers utilize telecommunications services for their own internal uses because such carriers would be end users for those services. This methodology is both competitively neutral and relatively easy to administer.

845. Basing contributions on end-user revenues, rather than gross revenues, is competitively neutral because it eliminates the problem of counting revenues derived from the same services twice. The double counting of revenues distorts competition because it disadvantages resellers. For example, assuming a 10 percent contribution rate on gross revenues, if facilities-based carrier X sells $200.00 worth of telecommunications services directly to a customer, its contribution will be $20.00. If reseller B buys $180.00 worth of wholesale services from carrier A and B sells the same retail services in competition with X after adding $20.00 of value, B would owe a contribution of $20.00 on these $200 worth of services, but B would also be required to recover the

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[2128] *See* Sprint comments at 9-10.

portion of the $18.00 contribution that A must make and would likely pass on to B. Therefore, while X would face $200.00 in service costs and $20.00 in support costs, B would face $200.00 in service costs and almost certainly substantially more than $20.00 in support costs. Adding another reseller to the A-B chain would compound this problem.

846. Assuming carriers will pass on some portion of the cost of contribution to their customers, the reseller, like B in the above example, that sells to end users will be disadvantaged vis-a-vis non-resellers of the same retail service, like X, because of this double-counting problem. We seek to avoid a contribution assessment methodology that distorts how carriers choose to structure their businesses or the types of services that they provide. Basing contributions on end-user revenues eliminates the double-counting problem and the market distortions assessments based on gross revenues create because transactions are only counted once at the end-user level. Although it will relieve wholesale carriers from contributing directly to the support mechanisms, the end-user method does not exclude wholesale revenues from the contribution base of carriers that sell to end users because wholesale charges are built into retail rates.

847. Consequently, we agree with the Joint Board's finding that basing contributions on gross telecommunications revenues creates a double-payment problem for resold services and thus is not competitively neutral, as discussed above. Therefore, like the Joint Board, we reject basing contributions on gross telecommunications revenues because that method is not consistent with the Joint Board's principle of competitive neutrality.

848. Calculating assessments based upon end-user telecommunications revenues also will be administratively easy to implement. Like the net telecommunications revenues approach, the end-user telecommunications revenues approach will require carriers to track their sales to end users; carriers, however, must already track their sales for billing purposes. Although the end-user telecommunications revenues method will require carriers to distinguish sales to end users from sales to resellers, we do not foresee that this will be difficult because resellers will have an incentive to notify wholesalers that they are purchasing services for resale in order to get a lower price that does not reflect universal service contribution requirements. Although the end-user telecommunications revenues approach requires that a distinction be made between retail and wholesale revenues, using end-user telecommunications revenues will still be easier to administer and less burdensome than the net telecommunications revenues approach because it will not require wholesale carriers to submit annual or monthly contributions directly to the administrator, as they would under the net telecommunications revenues approach. If wholesale carriers were required to make direct contributions based on their net telecommunications revenues, we would anticipate that they would try to pass that cost on to their carrier customers that provide retail services. Finally, although the Commission does not currently collect data regarding end-user telecommunications revenues, we are confident of our ability to develop a database of such information relatively quickly. In addition, we find that the Commission will be able to identify

inaccurate end-user-revenue filings based on revenue information in our existing databases.

849. Another reason we adopt an end-user telecommunications revenues method of assessing contributions rather than a net telecommunications revenues method is that, although the two methods are theoretically equivalent, the former method eliminates some economic distortions associated with the latter method that can occur in practice. As an initial matter, we observe that, contrary to some commenters' assertions, both methods are competitively neutral because they both eliminate double-counting of revenues and assess the same total amount of contributions. This is illustrated best with an example. Assume an IXC earned $100.00 in long distance revenues and paid $40.00 to a LEC in access charges. Assuming a hypothetical 10 percent contribution rate, under the end-user telecommunications revenues method, the IXC would be required to contribute $10.00 and the LEC would contribute nothing because it has no end-user telecommunications revenues. Under the net telecommunications revenues approach, the LEC would be required to contribute $4.00, and the IXC $6.00. Thus, under either method, the Commission would collect $10.00 in universal service contributions.

850. Although the two assessment methods are theoretically equivalent, we conclude that, in practice, the net telecommunications revenues approach is likely to cause distortions that could be avoided by using the end-user telecommunications revenues approach. For example, the theoretical equivalence of the two methods assumes that all carriers will be able to recover fully their

contributions from their customers. Some carriers, however, particularly those with long-term contracts, may be unable to recover fully those costs. If contributions are assessed on the basis of net telecommunications revenues and some intermediate carriers cannot incorporate their contributions into their prices, uneconomic substitution could result because other carriers would have an incentive to purchase services from those intermediate carriers, rather than to provide those services with their own facilities, to reduce their direct contribution to universal service. Basing contributions on end-user telecommunications revenues eliminates this potential economic distortion because contributions will be assessed at the end-user level, not at the wholesale and end-user level. Contributors will not have more of an incentive to build their own facilities or purchase services for resale in order to reduce their contribution because, regardless of how the services are provided, their contributions will be assessed only on revenues derived from end users.

851. In response to PacTel's request that the Commission clarify the Joint Board's discussion of universal service contributions and unbundled network elements,[2129] we state that ILECs are prohibited from incorporating universal service support into rates for unbundled network elements because universal service contributions are not part of the forward-looking costs of providing unbundled network elements.[2130] Although we

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[2129] PacTel comments at 26-27.

[2130] *See also Local Competition Order*, 11 FCC Rcd at 15860-15861. We note that the pricing provisions of the *Local Competition Order* are subject to a partial stay. *See supra* note 7.

do not mandate that carriers recover contributions in a particular manner, we note that carriers are permitted to pass through their contribution requirements to all of their customers of interstate services in an equitable and nondiscriminatory fashion.[2131] Furthermore, we find that universal service contributions constitute a sufficient public interest rationale to justify contract adjustments.[2132] Section 254 gives the Commission authority to require new contributions to the universal service support mechanisms from telecommunications carriers that provide interstate telecommunications services and other providers of interstate telecommunications. As discussed above, contributions will be assessed against revenues derived from end users for telecommunications or telecommunications services. Some of those revenues will be derived from private contractual agreements. By assessing a new contribution requirement, we create an expense or cost of doing business that was not anticipated at the time contracts were signed. Thus, we find that it would serve the public interest to allow telecommunications carriers and providers to make changes to existing contracts for service in order to adjust for this new cost of doing business. We clarify, however, that this finding is not intended to pre-empt state contract laws.

[2131] For further discussion of recovery issues, *see infra* section XIII.F.

[2132] *See United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) (finding that gas companies cannot change contract prices at will but the Federal Power Commission can authorize rate increases if it finds contract rates to conflict with the public interest).

852. We do not adopt commenters' suggestions that contributions be calculated entirely on non-revenues-based measures, such as a per-minute or per-line basis at this time.[2133] We affirm the Joint Board's recommendation that such mechanisms would require the Commission to adopt and administer difficult "equivalency ratios" for calculating the contributions of carriers that do not offer services on a per-line or per-minute basis.[2134] As competition changes the telecommunications marketplace, carriers may increasingly offer bundled services for flat-rate monthly charges. It would be administratively difficult to calculate an equivalent per-minute contribution for carriers that do not charge customers on a per-minute basis. In addition, we find that these approaches are not competitively neutral because they may inadvertently favor certain services or providers over others if the "equivalency ratios" are improperly calculated or inaccurate.

853. Furthermore, we agree with the Joint Board and reject commenters' suggestions that the Commission mandate that carriers recover contributions through an end-user surcharge.[2135] The state Joint Board members

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[2133] *See, e.g.*, APC comments at 9; Aerial comments at 2-3 (basing on per-line or number of dialable numbers is easily quantifiable and understood); Broadband PCS Alliance comments at 2-3 (arguing in favor of a charge based on number of lines); Sprint PCS comments at 10-11 (arguing in favor of a charge based on the number of subscribers served); AirTouch reply comments at 15-16 (arguing in favor of a charge based on each access line).

[2134] *See* Recommended Decision, 12 FCC Rcd at 496.

[2135] *See, e.g.*, ALLTEL comments at 8; Ameritech comments at 31; AT&T comments at 8; BellSouth comments at 15-16;

also assert that state commissions "should have the discretion to determine if the imposition of an end-user surcharge would render local rates unaffordable."[2136] A federally prescribed end-user surcharge would dictate how carriers recover their contribution obligations and would violate Congress's mandate and the wish of the state members of the Joint Board.[2137] The state Joint Board members add that it would be "premature" to judge how carriers in the telecommunications market would choose to recover their contributions during the transition to competitive markets.[2138] We agree with the state members and CPI that we should allow carriers the flexibility to decide how they should recover their contribution.[2139] As telecommunications carriers and providers begin merging telecommunications products into single offerings, for

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California Department of Consumer Affairs comments at 38-40; GTE comments at 36; LCI comments at 14; MFS comments at 112-13; NYNEX comments at 23-24; PacTel comments at 20-23; PageNet comments at 16; RTC comments at 35-36; SBC comments at 11-14; TDS comments at 6-8; U S West comments at 45-46; USTA comments at 22; WorldCom comments at 40-41; ACTA reply comments at 6; AirTouch reply comments at 20-21; ALTS reply comments at 5-8; BANX joint reply comments at 2-3; California SBA reply comments at 4-5; KMC reply comments at 4; SBC reply comments at 2-3.

[2136] State Members of the Federal-State Joint Board on Universal Service Comments on Recovery Mechanism for Universal Service Contributions, dated April 8, 1997, at 1 (*State Contributions Comments*).

[2137] *State Contribution Comments* at 1.

[2138] *State Contributions Comments* at 1.

[2139] CPI reply comments at 15-17.

example package prices for local and long distance service, we anticipate that they will offer bundled services and new pricing options. Mandating recovery through an end-user surcharge would eliminate carriers' pricing flexibility to the detriment of consumers.

854. In summary, we find the end-user telecommunications revenues approach to be more consistent with our principle of competitive neutrality than the gross revenues approach and easier to administer than the net telecommunications revenues approach. In addition, we agree with the state Joint Board members that an end-user surcharge is not necessary to ensure that contributions be explicit.[2140] We find that basing contributions on end-user telecommunications revenues satisfies the statutory requirement that support be explicit because carriers will know exactly how much they are contributing to the support mechanisms. Carriers will calculate their contributions by multiplying their end-user revenues by the universal service contribution percentage announced by the Commission or administrator, so there will be no ambiguity regarding the cost associated with the preservation and advancement of universal service.

855. To the extent that carriers seek to pass all or part of their contributions on to their customers in customer bills, we wish to ensure that carriers include complete and truthful information regarding the contribution amount. We do not assume that contributors will provide false or misleading statements, but we are concerned that consumers receive complete information regarding the

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[2140] *State Contributions Comments* at 2.

nature of the universal service contribution.[2141] Unlike the SLC,[2142] the universal service contribution is not a federally mandated direct end-user surcharge. We believe that it would be misleading for a carrier to characterize its contribution as a surcharge. Specifically, we believe that characterizing the mechanism as a surcharge would be misleading because carriers retain the flexibility to structure their recovery of the costs of universal service in many ways, including creating new pricing plans subject to monthly fees. As competition intensifies in the markets for local and interexchange services in the wake of the 1996 Act, it will likely lessen the ability of carriers and other providers of telecommunications to pass through to customers some or all of the former's contribution to the universal service mechanisms. If contributors, however, choose to pass through part of their contributions and to specify that fact on customers' bills, contributors must be careful to convey information in a manner that does not mislead by omitting important information that indicates that the contributor has chosen

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[2141] *See Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council*, 425 U.S. 748, 761 (1976). *See also Zauderer v. Office of Disciplinary Counsel of the Supreme Court of Ohio*, ___ U.S. ___, 105 S. Ct. 2265, 2281 (1985) (State may seek to prevent potential deception by requiring attorneys to disclose in their advertising certain factual information regarding fee arrangements); *see generally 44 Liquormart, Inc. v. Rhode Island*, ___ U.S. ___, 116 S. Ct. 1495, 1505 (1996).

[2142] *See* MTS and WATS Market Structure, *Third Report and Order*, 93 FCC 2d 241, *modified on recon., Memorandum Opinion and Order*, 97 FCC 2d 682 (1983).

to pass through the contribution or part of the contribution to its customers and that accurately describes the nature of the charge.

856. In addition, we agree with the Joint Board and TCA, which recommend that, if carriers provide services eligible for support from universal service support mechanisms at a discount or below cost, carriers may receive credits against their contributions.[2143] Contributions to the support mechanisms may be made in cash. In addition, carriers that provide services to eligible schools, libraries, or rural health care providers may offset their required contribution by an amount equal to the difference between the pre-discount price for service and the amount charged to the eligible institution. Allowing or requiring an offset will not prevent carriers from recovering the full, pre-offset contribution due on its revenues in the manner in which the carrier chooses.

857. Finally, we agree with SNET that carriers should not include support mechanisms payments when calculating their contributions.[2144] We find that payments received from the universal service support mechanisms do not qualify as revenues derived from end users for telecommunications revenues and should not be included in the assessment base. Finally, in response to Excel's comments that resellers should receive credits against their universal service contributions for the provision of supported services,[2145] we note that "pure" resellers may

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[2143] TCA comments at 9.

[2144] SNET comments at 4.

[2145] Excel comments at 15-16.

not be designated as "eligible carriers" under section 214(e) and may not receive universal service support payments.[2146] Carriers selling supported services to resellers, however, may be eligible to receive universal service support. In addition, carriers that offer supported services through the use of unbundled network elements, in whole or in part, may be eligible to receive universal service support.

[2146] 47 U.S.C. § 214(e). *See supra* section XI.B.2.b.

APPENDIX D

47 U.S.C. § 151. Purposes of chapter; Federal Communications Commission created

For the purpose of regulating interstate and foreign commerce in communication by wire and radio so as to make available, so far as possible, to all the people of the United States, without discrimination on the basis of race, color, religion, national origin, or sex, a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges, for the purpose of the national defense, for the purpose of promoting safety of life and property through the use of wire and radio communications, and for the purpose of securing a more effective execution of this policy by centralizing authority heretofore granted by law to several agencies and by granting additional authority with respect to interstate and foreign commerce in wire and radio communication, there is created a commission to be known as the "Federal Communications Commission", which shall be constituted as hereinafter provided, and which shall execute and enforce the provisions of this chapter.

47 U.S.C. § 152(b)

(b) Exceptions to Federal Communications Commission jurisdiction

Except as provided in sections 223 through 227 of this title, inclusive, and section 332 of this title, and subject to the provisions of section 301 of this title and subchapter V-A of this chapter, nothing in this chapter shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier, or (2) any carrier engaged in interstate or foreign communication solely through physical connection with the facilities of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with such carrier, or (3) any carrier engaged in interstate or foreign communication solely through connection by radio, or by wire and radio, with facilities, located in an adjoining State or in Canada or Mexico (where they adjoin the State in which the carrier is doing business), of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with such carrier, or (4) any carrier to which clause (2) or clause (3) of this subsection would be applicable except for furnishing interstate mobile radio communication service or radio communication service to mobile stations on land vehicles in Canada or Mexico; except that sections 201 to 205 of this title shall, except as otherwise provided therein, apply to carriers described in clauses (2), (3), and (4) of this subsection.

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47 U.S.C. § 201. Service and charges

(a) It shall be the duty of every common carrier engaged in interstate or foreign communication by wire or radio to furnish such communication service upon reasonable request therefor; and, in accordance with the orders of the Commission, in cases where the Commission, after opportunity for hearing, finds such action necessary or desirable in the public interest, to establish physical connections with other carriers, to establish through routes and charges applicable thereto and the divisions of such charges, and to establish and provide facilities and regulations for operating such through routes.

(b) All charges, practices, classifications, and regulations for and in connection with such communication service, shall be just and reasonable, and any such charge, practice, classification, or regulation that is unjust or unreasonable is declared to be unlawful: *Provided*, That communications by wire or radio subject to this chapter may be classified into day, night, repeated, unrepeated, letter, commercial, press, Government, and such other classes as the Commission may decide to be just and reasonable, and different charges may be made for the different classes of communications: *Provided further*, That nothing in this chapter or in any other provision of law shall be construed to prevent a common carrier subject to this chapter from entering into or operating under any contract with any common carrier not subject to this chapter, for the exchange of their services, if the Commission is of the opinion that such contract is not contrary to the public interest: *Provided further*, That nothing in this chapter or in any other provision of law shall prevent a

common carrier subject to this chapter from furnishing reports of positions of ships at sea to newspapers of general circulation, either at a nominal charge or without charge, provided the name of such common carrier is displayed along with such ship position reports. The Commission may prescribe such rules and regulations as may be necessary in the public interest to carry out the provisions of this chapter.

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§ 252. Procedures for negotiation, arbitration, and approval of agreements

(a) Agreements arrived at through negotiation

(1) Voluntary negotiations

Upon receiving a request for interconnection, services, or network elements pursuant to section 251 of this title, an incumbent local exchange carrier may negotiate and enter into a binding agreement with the requesting telecommunications carrier or carriers without regard to the standards set forth in subsections (b) and (c) of section 251 of this title. The agreement shall include a detailed schedule of itemized charges for interconnection and each service or network element included in the agreement. The agreement, including any interconnection agreement negotiated before February 8, 1996, shall be submitted to the State commission under subsection (e) of this section.

(2) Mediation

Any party negotiating an agreement under this section may, at any point in the negotiation, ask a State commission to participate in the negotiation and to mediate any differences arising in the course of the negotiation.

(b) Agreements arrived at through compulsory arbitration

(1) Arbitration

During the period from the 185th to the 160th day (inclusive) after the date on which an incumbent local exchange carrier receives a request for negotiation under this section, the carrier or any other party to the negotiation may petition a State commission to arbitrate any open issues.

(2) Duty of petitioner

(A) A party that petitions a State commission under paragraph (1) shall, at the same time as it submits the petition, provide the State commission all relevant documentation concerning –

(i) the unresolved issues;

(ii) the position of each of the parties with respect to those issues; and

(iii) any other issue discussed and resolved by the parties.

(B) A party petitioning a State commission under paragraph (1) shall provide a copy of the petition and any documentation to the other party or parties not later than the day on which the State commission receives the petition.

(3) Opportunity to respond

A non-petitioning party to a negotiation under this section may respond to the other party's petition and provide such additional information as it wishes within 25 days after the State commission receives the petition.

(4) Action by State commission

(A) The State commission shall limit its consideration of any petition under paragraph (1) (and any response thereto) to the issues set forth in the petition and in the response, if any, filed under paragraph (3).

(B) The State commission may require the petitioning party and the responding party to provide such information as may be necessary for the State commission to reach a decision on the unresolved issues. If any party refuses or fails unreasonably to respond on a timely basis to any reasonable request from the State commission, then the State commission may proceed on the basis of the best information available to it from whatever source derived.

(C) The State commission shall resolve each issue set forth in the petition and the response, if any, by imposing appropriate conditions as required to implement subsection (c) of this section upon the parties to the agreement, and shall conclude the resolution of any unresolved issues not later than 9 months after the date on which the local exchange carrier received the request under this section.

(5) Refusal to negotiate

The refusal of any other party in the negotiation to participate further in the negotiation,

to cooperate with the State commission in carrying out its function as an arbitrator, or to continue to negotiate in good faith in the presence, or with the assistance, of the State commission shall be considered a failure to negotiate in good faith.

(c) Standards for arbitration

In resolving by arbitration under subsection (b) of this section any open issues and imposing conditions upon the parties to the agreement, a State commission shall –

(1) ensure that such resolution and conditions meet the requirements of section 251 of this title, including the regulations prescribed by the Commission pursuant to section 251 of this title;

(2) establish any rates for interconnection, services, or network elements according to subsection (d) of this section; and

(3) provide a schedule for implementation of the terms and conditions by the parties to the agreement.

(d) Pricing standards

(1) Interconnection and network element charges

Determinations by a State commission of the just and reasonable rate for the interconnection of facilities and equipment for purposes of subsection (c)(2) of section 251 of this title, and the just and reasonable rate for network elements for purposes of subsection (c)(3) of such section –

(A) shall be –

(i) based on the cost (determined without reference to a rate-of-return or other rate-based proceeding) of providing the interconnection or network element (whichever is applicable), and

(ii) nondiscriminatory, and

(B) may include a reasonable profit.

(2) Charges for transport and termination of traffic

(A) In general

For the purposes of compliance by an incumbent local exchange carrier with section 251(b)(5) of this title, a State commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable unless –

(i) such terms and conditions provide for the mutual and reciprocal recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier; and

(ii) such terms and conditions determine such costs on the basis of a reasonable approximation of the additional costs of terminating such calls.

(B) Rules of construction

This paragraph shall not be construed –

(i) to preclude arrangements that afford the mutual recovery of costs

through the offsetting of reciprocal obligations, including arrangements that waive mutual recovery (such as bill-and-keep arrangements); or

(ii) to authorize the Commission or any State commission to engage in any rate regulation proceeding to establish with particularity the additional costs of transporting or terminating calls, or to require carriers to maintain records with respect to the additional costs of such calls.

(3) Wholesale price for telecommunications services

For the purposes of section 251(c)(4) of this title, a State commission shall determine wholesale rates on the basis of retail rates charges to subscribers for the telecommunications service requested, excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier.

(e) Approval by State commission

(1) Approval required

Any interconnection agreement adopted by negotiation or arbitration shall be submitted for approval to the State commission. A State commission to which an agreement is submitted shall approve or reject the agreement, with written findings as to any deficiencies.

(2) Grounds for rejection

The State commission may only reject.

(A) an agreement for any portion thereof) adopted by negotiation under subsection (a) of this section if it finds that –

(i) the agreement (or portion thereof) discriminates against a telecommunications carrier not a party to the agreement; or

(ii) the implementation of such agreement or portion is not consistent with the public interest, convenience, and necessity; or

(B) an agreement (or any portion thereof) adopted by arbitration under subsection (b) of this section if it finds that the agreement does not meet the requirements of section 251 of this title, including the regulations prescribed by the Commission pursuant to section 251 of this title, or the standards set forth in subsection (d) of this section.

(3) Preservation of authority

Notwithstanding paragraph (2), but subject to section 253 of this title, nothing in this section shall prohibit a State commission from establishing or enforcing other requirements of State law in its review of an agreement, including requiring compliances with intrastate telecommunications service quality standards or requirements.

(4) Schedule for decision

If the State commission does not act to approve or reject the agreement within 90 days after submission by the parties of an agreement adopted by negotiation under subsection (a) of this section, or within 30 days after submission

by the parties of an agreement adopted by arbitration under subsection (b) of this section, the agreement shall be deemed approved. No State court shall have jurisdiction to review the action of a State commission in approving or rejecting an agreement under this section.

(5) Commission to act if State will not act

If a State commission fails to act to carry out its responsibility under this section in any proceeding or other matter under this section, then the Commission shall issue an order preempting the State commission's jurisdiction of that proceeding or matter within 90 days after being notified (or taking notice) of such failure, and shall assume the responsibility of the State commission under this section with respect to the proceeding or matter and act for the State commission.

(6) Review of State commission actions

In a case in which a State fails to act as described in paragraph (5), the proceeding by the Commission under such paragraph and any judicial review of the Commission's actions shall be the exclusive remedies for a State commission's failure to act. In any case in which a State commission makes a determination under this section, any party aggrieved by such determination may bring an action in an appropriate Federal district court to determine whether the agreement or statement meets the requirements of section 251 of this title and this section.

(f) Statements of generally available terms

(1) In general

A Bell operating company may prepare and file with a State commission a statement of the terms and conditions that such company generally offers within that State to comply with the requirements of section 251 of this title and the regulations thereunder and the standards applicable under this section.

(2) State commission review

A State commission may not approve such statement unless such statement complies with subsection (d) of this section and section 251 of this title and the regulations thereunder. Except as provided in section 253 of this title, nothing in this section shall prohibit a State commission from establishing or enforcing other requirements of State law in its review of such statement, including requiring compliance with intrastate telecommunications service quality standards or requirements.

(3) Schedule for review

The State commission to which a statement is submitted shall, not later than 60 days after the date of such submission –

(A) complete the review of such statement under paragraph (2) (including any reconsideration thereof), unless the submitting carrier agrees to an extension of the period for such review; or

(B) permit such statement to take effect.

(4) Authority to continue review

Paragraph (3) shall not preclude the State commission from continuing to review a statement that has been permitted to take effect under subparagraph (B) of such paragraph or from approving or disapproving such statement under paragraph (2).

(5) Duty to negotiate not affected

The submission or approval of a statement under this subsection shall not relieve a Bell operating company of its duty to negotiate the terms and conditions of an agreement under section 251 of this title.

(g) Consolidation of State proceedings

Where not inconsistent with the requirements of this chapter, a State commission may, to the extent practical, consolidate proceedings under sections 214(e), 251(f), and 253 of this title, and this section in order to reduce administrative burdens on telecommunications carriers, other parties to the proceedings, and the State commission in carrying out its responsibilities under this chapter.

(h) Filing required

A State commission shall make a copy of each agreement approved under subsection (e) of this section and each statement approved under subsection (f) of this section available for public inspection and copying within 10 days after the agreement or statement is approved. The State commission may charge a reasonable and nondiscriminatory fee to the parties to the agreement or to the party filing the statement to cover the costs of approving and filing such agreement or statement.

(i) Availability to other telecommunications carriers

A local exchange carrier shall make available any interconnection, service, or network element provided under an agreement approved under this section to which it is a party to any other requesting telecommunications carrier upon the same terms and conditions as those provided in the agreement.

(j) Definition of incumbent local exchange carrier

For purposes of this section, the term "incumbent local exchange carrier" has the meaning provided in section 251(b) of this title.

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47 U.S.C. § 254. Universal service

(a) Procedures to review universal service requirements

(1) Federal-State Joint Board on universal service

Within one month after February 8, 1996, the Commission shall institute and refer to a Federal-State Joint Board under section 410(c) of this title a proceeding to recommend changes to any of its regulations in order to implement sections 214(e) of this title and this section, including the definition of the services that are supported by Federal universal service support mechanisms and a specific timetable for completion of such recommendations. In addition to the members of the Joint Board required under section 410(c) of this title, one member of such

Joint Board shall be a State-appointed utility consumer advocate nominated by a national organization of State utility consumer advocates. The Joint Board shall, after notice and opportunity for public comment, make its recommendations to the Commission 9 months after February 8, 1996.

(2) Commission action

The Commission shall initiate a single proceeding to implement the recommendations from the Joint Board required by paragraph (1) and shall complete such proceeding within 15 months after February 8, 1996. The rules established by such proceeding shall include a definition of the services that are supported by Federal universal service support mechanisms and a specific timetable for implementation. Thereafter, the Commission shall complete any proceeding to implement subsequent recommendations from any Joint Board on universal service within one year after receiving such recommendations.

(b) Universal service principles

The Joint Board and the Commission shall base policies for the preservation and advancement of universal service on the following principles:

(1) Quality and rates

Quality services should be available at just, reasonable, and affordable rates.

(2) Access to advanced services

Access to advanced telecommunications and information services should be provided in all regions of the Nation.

(3) Access in rural and high cost areas

Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.

(4) Equitable and nondiscriminatory contributions

All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service.

(5) Specific and predictable support mechanisms

There should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service.

(6) Access to advanced telecommunications services for schools, health care, and libraries

Elementary and secondary schools and classrooms, health care providers, and libraries should have access to advanced telecommunications services as described in subsection (h) of this section.

(7) Additional principles

Such other principles as the Joint Board and the Commission determine are necessary and

appropriate for the protection of the public interest, convenience, and necessity and are consistent with this chapter.

(c) Definition

(1) In general

Universal service is an evolving level of telecommunications services that the Commission shall establish periodically under this section, taking into account advances in telecommunications and information technologies and services. The Joint Board in recommending, and the Commission in establishing, the definition of the services that are supported by Federal universal service support mechanisms shall consider the extent to which such telecommunications services –

(A) are essential to education, public health, or public safety;

(B) have, through the operation of market choices by customers, been subscribed to by a substantial majority of residential customers;

(C) are being deployed in public telecommunications networks by telecommunications carriers; and

(D) are consistent with the public interest, convenience, and necessity.

(2) Alterations and modifications

The Joint Board may, from time to time, recommend to the Commission modifications in the definition of the services that are supported by Federal universal service support mechanisms.

(3) Special services

In addition to the services included in the definition of universal service under paragraph (1), the Commission may designate additional services for such support mechanisms for schools, libraries, and health care providers for the purposes of subsection (h) of this section.

(d) Telecommunications carrier contribution

Every telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service. The Commission may exempt a carrier or class of carriers from this requirement if the carrier's telecommunications activities are limited to such an extent that the level of such carrier's contribution to the preservation and advancement of universal service would be de minimis. Any other provider of interstate telecommunications may be required to contribute to the preservation and advancement of universal service if the public interest so requires.

(e) Universal service support

After the date on which Commission regulations implementing this section take effect, only an eligible telecommunications carrier designated under section 214(e) of this title shall be eligible to receive specific Federal universal service support. A carrier that receives such support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. Any such

support should be explicit and sufficient to achieve the purposes of this section.

(f) State authority

A State may adopt regulations not inconsistent with the Commission's rules to preserve and advance universal service. Every telecommunications carrier that provides intrastate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, in a manner determined by the State to the preservation and advancement of universal service in that State. A State may adopt regulations to provide for additional definitions and standards to preserve and advance universal service within that State only to the extent that such regulations adopt additional specific, predictable, and sufficient mechanisms to support such definitions or standards that do not rely on or burden Federal universal service support mechanisms.

(g) Interexchange and interstate services

Within 6 months after February 8, 1996, the Commission shall adopt rules to require that the rates charged by providers of interexchange telecommunications services to subscribers in rural and high cost areas shall be no higher than the rates charged by each such provider to its subscribers in urban areas. Such rules shall also require that a provider of interstate interexchange telecommunications services shall provide such services to its subscribers in each State at rates no higher than the rates charged to its subscribers in any other State.

(h) Telecommunications services for certain providers

(1) In general

(A) Health care providers for rural areas

A telecommunications carrier shall, upon receiving a bona fide request, provide telecommunications services which are necessary for the provision of health care services in a State, including instruction relating to such services, to any public or nonprofit health care provider that serves persons who reside in rural areas in that State at rates that are reasonably comparable to rates charged for similar services in urban areas in that State. A telecommunications carrier providing service under this paragraph shall be entitled to have an amount equal to the difference, if any, between the rates for services provided to health care providers for rural areas in a State and the rates for similar services provided to other customers in comparable rural areas in that State treated as a service obligation as a part of its obligation to participate in the mechanisms to preserve and advance universal service.

(B) Educational providers and libraries

All telecommunications carriers serving a geographic area shall, upon a bona fide request for any of its services that are within the definition of universal service under subsection (c)(3) of this section, provide such services to elementary schools, secondary schools, and libraries for educational purposes at rates less than the amounts charged for similar services to

other parties. The discount shall be an amount that the Commission, with respect to interstate services, and the States, with respect to intrastate services, determine is appropriate and necessary to ensure affordable access to and use of such services by such entities. A telecommunications carrier providing service under this paragraph shall –

(i) have an amount equal to the amount of the discount treated as an offset to its obligation to contribute to the mechanisms to preserve and advance universal service, or

(ii) notwithstanding the provisions of subsection (e) of this section, receive reimbursement utilizing the support mechanisms to preserve and advance universal service.

(2) Advanced services

The Commission shall establish competitively neutral rules –

(A) to enhance, to the extent technically feasible and economically reasonable, access to advanced telecommunications and information services for all public and nonprofit elementary and secondary school classrooms, health care providers, and libraries; and

(B) to define the circumstances under which a telecommunications carrier may be required to connect its network to such public institutional telecommunications users.

(3) Terms and conditions

Telecommunications services and network capacity provided to a public institutional telecommunications user under this subsection may not be sold, resold, or otherwise transferred by such user in consideration for money or any other thing of value.

(4) Eligibility of users

No entity listed in this subsection shall be entitled to preferential rates or treatment as required by this subsection, if such entity operates as a for-profit business, is a school described in paragraph (5)(A) with an endowment of more than $50,000,000, or is a library or library consortium not eligible for assistance from a State library administrative agency under the Library Services and Technology Act [20 U.S.C.A. 9121 et seq.].

(5) Definitions

For purposes of this subsection:

(A) Elementary and secondary schools

The term "elementary and secondary schools" means elementary schools and secondary schools, as defined in paragraphs (14) and (25), respectively, of section 8801 of title 20.

(B) Health care provider

The term "health care provider" means –

(i) post-secondary educational institutions offering health care instruction, teaching hospitals, and medical schools;

(ii) community health centers or health centers providing health care to migrants;

(iii) local health departments or agencies;

(iv) community mental health centers;

(v) not-for-profit hospitals;

(vi) rural health clinics; and

(vii) consortia of health care providers consisting of one or more entities described in clauses (i) through (vi).

(C) Public institutional telecommunications user

The term "public institutional telecommunications user" means an elementary or secondary school, a library, or a health care provider as those terms are defined in this paragraph.

(i) Consumer protection

The Commission and the States should ensure that universal service is available at rates that are just, reasonable, and affordable.

(j) Lifeline assistance

Nothing in this section shall affect the collection, distribution, or administration of the Lifeline Assistance Program provided for by the Commission under regulations set forth in section 69.117 of title 47, Code of Federal Regulations, and other related sections of such title.

(k) Subsidy of competitive services prohibited

A telecommunications carrier may not use services that are not competitive to subsidize services that are subject to competition. The Commission, with respect to interstate services, and the States, with respect to intrastate services, shall establish any necessary cost allocation rules, accounting safeguards, and guidelines to ensure that services included in the definition of universal service bear no more than a reasonable share of the joint and common costs of facilities used to provide those services.